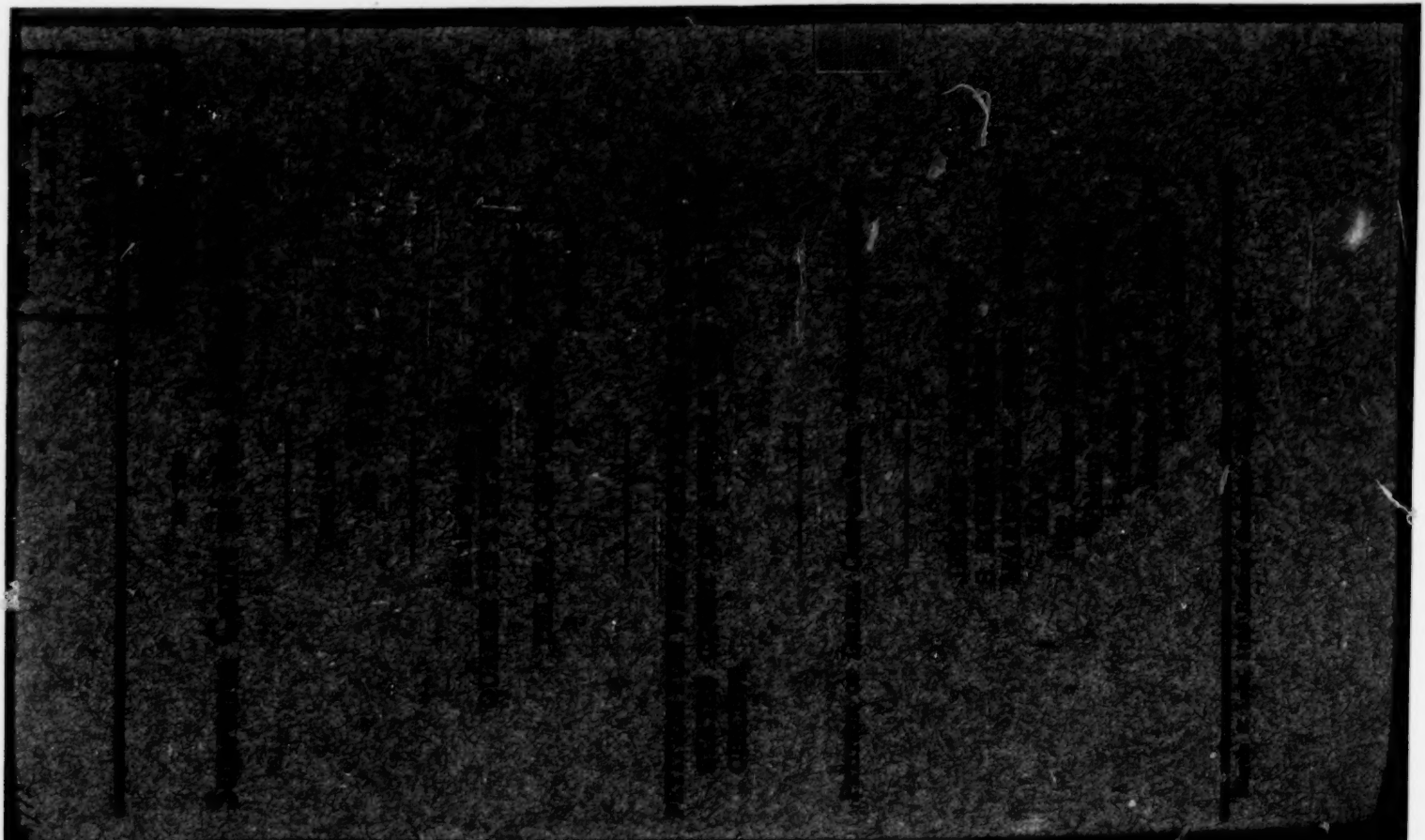

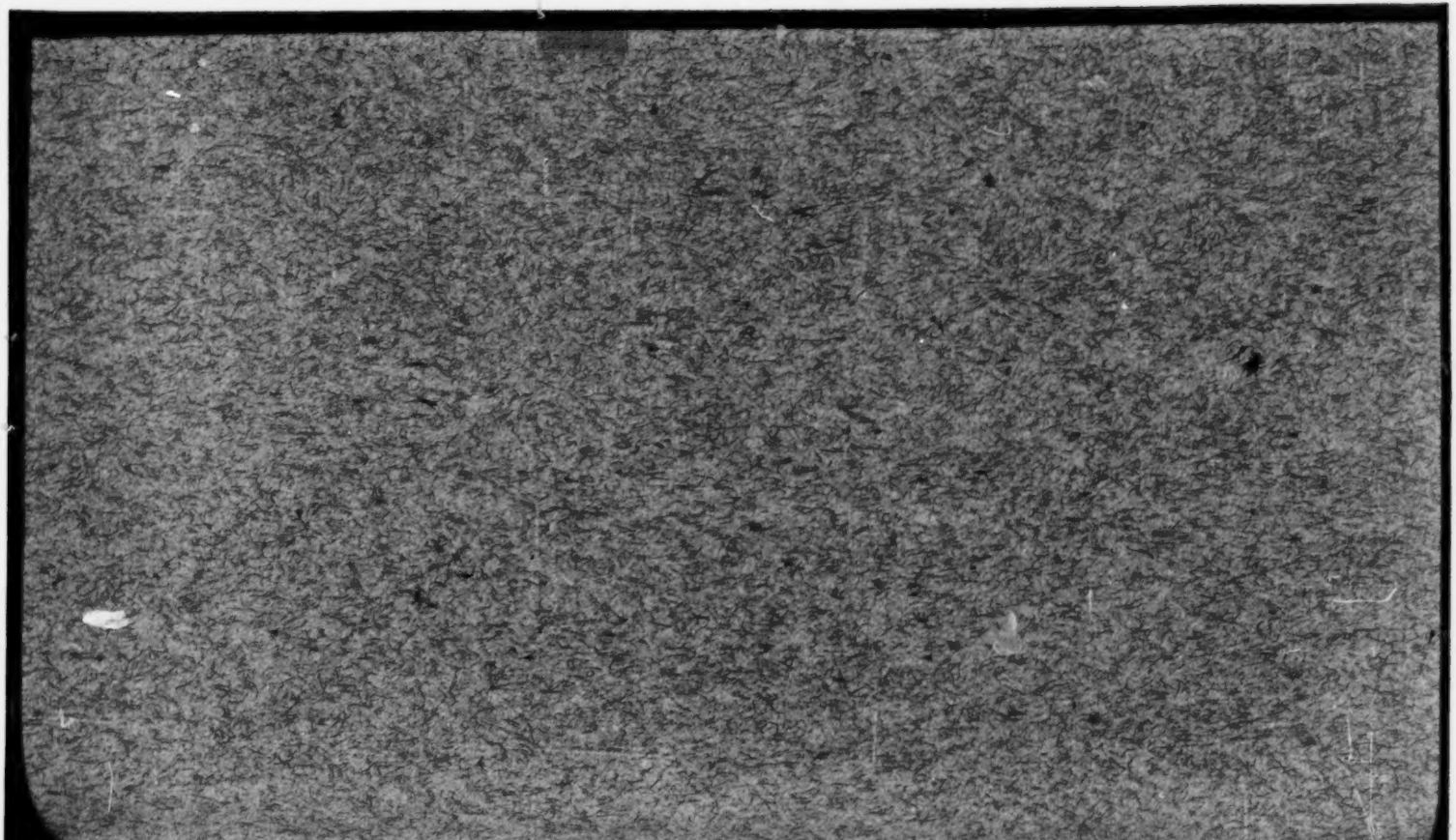

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IN THE

SUPREME COURT OF THE UNITED STATES.

Term, 1957.

No.

In the Matter of
QUAKER CITY UNIFORM CO., INC.,
Bankrupt,
DELSEA CORPORATION,
Petitioner.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

TO THE HONORABLE, THE CHIEF JUSTICE OF THE UNITED STATES AND ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

Delsea Corporation prays that a Writ of Certiorari issue to review the judgment of the United States Court of Appeals for the Third Circuit entered in the above entitled case on October 31, 1956.

I. CITATIONS TO OPINIONS BELOW.

The opinion of the Referee in Bankruptcy (R. p. 14a) is unreported.

The opinion of the District Court (R. p. 24a) is reported in 134 F. Supp. 596 (1955).

The opinion of the Court of Appeals was entered on July 27, 1956 and is unofficially reported in 135 Legal Intelligencer No. 25, p. 1, column 3 and is printed in appendix hereto infra, p. 13. Following the granting of a timely Petition for Reargument that opinion was withdrawn and on October 31, 1956 an opinion was entered, printed in appendix hereto infra, p. 19 and is as yet unreported.

II. JURISDICTION.

The judgment of the Court of Appeals was entered on October 31, 1956 printed in appendix hereto infra, p. 19. The jurisdiction of this Court is invoked under 62 Stat. 928 (1948), 28 U. S. C. §1254 and 66 Stat. 423 (1952), 11 U. S. C. §47c.

III. QUESTION PRESENTED.

Did Congress by Section 67c of the Bankruptcy Act (52 Stat. 875 (1938), 11 U. S. C. §107c) mean to establish priorities in or to deal with property which formed no part of the assets administrable in bankruptcy so that a chattel mortgage, which by State law is subordinate to a landlord's distraint, loses its lien thereby, and the proceeds of the mortgaged chattels become part of the Bankrupt Estate and distributable in accordance with the priorities of Section 64 of the Bankruptcy Act?

IV. STATUTE INVOLVED.

The statutory provisions involved are Sections 64a and 67c of the Bankruptcy Act 52 Stat. 874 and 875 (1938), 11 U. S. C. §§104a and 107c. They are printed in appendix hereto infra, pages 10 to 12 inclusive.

V. STATEMENT.

An involuntary petition in bankruptcy was filed against Quaker City Uniform Company on July 16, 1953 (R. p. 1a). The jurisdiction of the District Court was invoked because the case arises under the Bankruptcy Act.

Prior to the bankruptcy, Delsea Corporation, as landlord made a distraint on May 12, 1953 on all the goods on the premises. The sale of the goods under the distraint was stayed under Pennsylvania law because execution was later issued by the sheriff on another debt of the tenant. Before the sheriff's sale was held, the involuntary petition in bankruptcy was filed.

Thereafter Daniel P. Veloric filed a Petition for Reclamation of certain goods subject to his chattel mortgage, which mortgage had been duly recorded over four (4) months prior to the bankruptcy. The landlord filed a Petition to Intervene claiming that the goods which were subject to the distraint should be turned over to it instead of the chattel mortgagee. The parties agreed by stipulation that the goods should be sold and the fund substituted. The question of the distribution of the fund arising from the sale of the goods subject to the Veloric chattel mortgage, as well as another chattel mortgage held by the Fidelity-Philadelphia Trust Company, was determined at the audit of the account of the Trustee. The parties stipulated all the facts and, after hearing, the Referee in Bankruptcy made an order of distribution in which he held that the chattel mortgage was valid and Veloric (as well as the other chattel mortgagee,

the Fidelity-Philadelphia Trust Company) entitled to the proceeds of the chattels up to the amount of the mortgage, but that the landlord was not entitled to share in that fund. Upon a Petition for Review the District Judge reversed the order of the priority with respect to the fund awarded Veloric, and sustained the landlord's Petition that the fund subject to the chattel mortgages was not a part of the assets of the Bankrupt Estate, and that it should be set aside for the chattel mortgagees. The District Court held that the chattels being on the premises were, in accordance with Pennsylvania law, subject to the prior lien of the landlord which should first be paid out of that fund. The District Court held that the Trustee in Bankruptcy had no interest in that fund arising out of a valid lien except to distribute it to the chattel mortgage, subject to the superior lien thereon. Veloric alone appealed. The Court of Appeals below reversed the order of distribution of the District Court.

The decision of the Court of Appeals was based, first upon the conclusion that a chattel mortgage was a "statutory lien"[1] within the provisions of Section 67c of the Bankruptcy Act and hence invalid. Upon reargument, however, the Court withdrew that opinion and held that it was not necessary to so decide because the lien of the chattel mortgage was subordinate to administration expenses, wages and taxes as it was subject to the landlord's lien under its distraint, and the attaching of the landlord's lien to the fund would advance the landlord's priority in contravention of the order of distribution provided by Section 64 of the Bankruptcy Act.[2] The Learned Court below held that no fund should be distributed to the chattel mortgage even

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[1] Chattel mortgages are "contractual" liens and not "statutory" liens: 4 Collier 14th Edition, pages 184, 268.

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[2] The Learned Court below while noting (opinion p. 5, note 4) that the chattel mortgages were created prior to the effective date of the amendment of 1952, failed to consider the effect of the clause in Section 67c (52 Stat. 876 (1938)): "* * * except as against other liens * * *" which would leave the distraint valid against the lien of the chattel mortgage.

though the rent claim was less than the amount of the chattel mortgage.

VI. REASONS FOR GRANTING THE WRIT.

1. The decision in this case has such a potentially far reaching effect on the methods of commercial financing that seven major Philadelphia banking institutions and the National Commercial Finance Conference, Inc. of New York intervened in the Court of Appeals proceedings as *amicus curiae*. It is estimated that more than five billion dollars worth of credit and financing arrangements will be adversely affected by the Court of Appeals' decision in this case.[3] Banking, credit and financing institutions have heretofore loaned vast sums of money secured by chattel mortgages and similar security agreements upon the widely accepted understanding of the law that the lien created by these various arrangements would take precedence, in the event of Bankruptcy, over the priorities enumerated in Section 64a of the Bankruptcy Act. As a result of the decision of the Court of Appeals in this case, these secured creditors find the lien upon which they depended rendered valueless for all practical purposes at the moment when they need it the most.

2. Clearly the question presented is of importance in the administration of the Federal Bankruptcy Law. This is a problem which arises in virtually every Bankrupt Estate.

The facts of this case involve the relative position of a landlord's lien, a chattel mortgage, costs of administration and wage claims. The landlord's lien is prior to the chattel mortgage under the law of the Commonwealth of Pennsylvania. A landlord's lien is postponed in payment to the costs of administration and wage claims by Section 67c of the Bankruptcy Act. This very factual situation arises with

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[3] See briefs of **amicus curiae** in Court of Appeals of banks and the National Commercial Finance Conference, Inc.

great frequency in Bankrupt Estates. Furthermore, the identical legal issues will be raised every time there is a coexistence in a Bankrupt Estate of statutory liens which are prior under the law of various states such as those in favor of employees, mechanics and contractors, etc., and those liens which arise from such financing arrangements as conditional sales, factoring agreements, trust receipts, etc. Virtually every Bankrupt Estate involves some combination of the foregoing claims, and thus will raise the issues presented by the instant case.

As a matter of fact, such an issue has already arisen and the Referee in Bankruptcy has followed the Court of Appeals' decision in the instant case. In the *Matter of George Townsend Co., Inc.*, No. 24446 Eastern District of Pennsylvania (unofficially reported in the Philadelphia Legal Intelligencer December 6, 1956), the Referee ruled that because there was an unpaid claim of a landlord without a prior distraint, the landlord, a chattel mortgagee and a conditional vendor were all subordinate to the costs of administration.

This case squarely raises the issue of the relative position of secured creditors, statutory liens, wage claims and the costs of administration. In so doing it requires a clear interpretation of the meaning of Section 67c of the Bankruptcy Act.

In spite of the potential monetary effect that this case has, and the frequency with which this issue arises, this case presents a question which is essentially one of first impression. To date there has not been a truly definitive decision which interprets Section 67c of the Bankruptcy Act.

3. It is submitted that the Court of Appeals has misconstrued the intention of Congress in regard to Section 67c of the Bankruptcy Act.

The Court of Appeals has written two opinions in this matter, the first of which has been withdrawn. In the first opinion the Court ruled that both the landlord's lien for rent and the lien of the chattel mortgage were statutory liens unaccompanied by possession and hence subordinated

to the costs of administration and wage claims by virtue of Section 67c of the Bankruptcy Act. The second opinion was based upon the assumption that the lien of a chattel mortgage was not a "statutory lien." The Court then concluded that the lien of the chattel mortgage was none the less subordinate to the costs of administration and wage claims because under the law of the Commonwealth of Pennsylvania it was inferior to the landlord's lien. The Learned Court below held that under Section 67c of the Bankruptcy Act the landlord's lien on the chattel mortgage was in turn postponed in payment to the priorities of Section 64a of the Bankruptcy Act. In so doing the Court ruled that the chattel mortgage was subordinated because Congress' primary intent in enacting Section 67c was to protect wage claimants and costs of administration. Because the chattels were subject to the landlord's distraint, the Learned Court below held that neither the landlord nor the chattel mortgagee were entitled to the security of the mortgage.

It is submitted that Congress meant to protect the costs of administration and wage claimants only in a situation where there was a fund available for distribution in which they were entitled to share. Except in that area there was no intent to in any way affect a lien which was valid and subsisting under State law. The assets upon which a secured creditor has a lien are not available for costs of administration or wage claims until the lien has been satisfied, and therefore Congress never intended that the liens of secured creditors should be affected by the existence of costs of administration and wage claims.

Your Petitioner submits that this Honorable Court must necessarily decide the question of the status of the lien of a chattel mortgage as a "statutory lien." In this respect the first decision of the Court of Appeals below is in conflict in principle with the rulings in *Ginsburg v. Lindel*, 107 F. 2nd 721 (8th Circuit 1939); *In Re: Telephone Radio Corporation*, 133 Fed. Supp. 739 (District Court New Jersey 1955). Both the above cited cases have held that liens created by se-

great frequency in Bankrupt Estates. Furthermore, the identical legal issues will be raised every time there is a coexistence in a Bankrupt Estate of statutory liens which are prior under the law of various states such as those in favor of employees, mechanics and contractors, etc., and those liens which arise from such financing arrangements as conditional sales, factoring agreements, trust receipts, etc. Virtually every Bankrupt Estate involves some combination of the foregoing claims, and thus will raise the issues presented by the instant case.

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curity agreements similar to chattel mortgages are not statutory liens.

4. The intent of Congress was, as discussed by his Honor Chief Judge Kirkpatrick in the Court below (appendix p. 25a), not to impair valid liens. The decision by the Court of Appeals is a sweeping change in the existing law and was not made by Congress expressly but was inferred by the Court below from the fact that a landlord would receive payment of his rent out of a fund which otherwise would be paid to the chattel mortgagee and was not a portion of the Bankrupt Estate. If Congress, when it passed the Chandler Act and its several amendments had wished to make this fundamental change with respect to priority of liens, it would have done so by specific enactment and in clear and unmistakable terms.

5. The decision of the Court below is in conflict with the Pennsylvania decisions which admittedly hold that the landlord's lien is superior to the chattel mortgage. *Commercial Credit Plan vs. Mahoney*, 67 Pa. D. & C. 577 (1948); *Reinhart vs. Gerhardt*, 152 Pa. Super. 229 (1943); *National Cash Register Co. vs. Ansell*, 125 Pa. Super. 309 (1937). The decision of the Learned Court below was based upon a rationale that the landlord would obtain an undue preference if the chattel mortgage were held to be valid under Section 67 of the Bankruptcy Act The error into which the Court below fell was based upon its failure to distinguish between assets in the Bankrupt Estate held by the Trustee which are distributable under Section 64,[4] and assets against which there is a valid lien which should be set aside under State law for distribution in the manner provided by State law.

The decision is in conflict with the holding of *In Re: Proudfoot* (Circuit Court N. D. West Virginia (1909), 173

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[4] The provisions of Section 64 of the Bankruptcy Act all pertain to the general assets of the estate "and have no relation to property which by reason of liens never became any part of the Bankrupt Estate:" **In Re: Hosmer** (District Court Iowa), 233 Fed. 218.

Fed. Rep. 733, which holds squarely that wages are not to be paid out of property subject to a valid state lien. The validity of the lien of chattel mortgages (valid under State law) has been upheld in *In Re: American Motor Products Corp.* (2nd Circuit 1938), 98 Fed. 2nd 774; *Lockhart vs. Garden City Bank and Trust Company* (2nd Circuit 1940), 116 F. 2nd 658.

6. Further if so well settled and fundamental an interpretation that a valid lien should remain valid unless changed by Congress requires alteration on the grounds of policy such as alleged injustice or hardship upon priority creditors, relief is not with the courts but with the legislature. Nothing in the reports of House Committee or the Senate Committee [5] indicated that Congress intended to invalidate liens valid under State law, for the benefit of administration expenses, wages, and taxes. The error of the opinion of the Court below is the failure to distinguish between the two separate priorities called for under the Bankruptcy Act: one a priority of lien, and the other a priority of distribution of assets properly includable in the Bankrupt Estate.

VII. CONCLUSION.

For the foregoing reasons this Petition for a Writ of Certiorari should be granted.

Respectfully submitted,

JEROME L. MARKOVITZ,
S. ROBERT LEVANT,
MARKOVITZ, STERN & SHUSTERMAN,
Attorneys for the Delsea Corporation, Petitioner.

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[5] House Committee Report No. 1293 on S. 88, 81st Congress 1st Session (1949) p. 3. House Committee Report No. 2320 on S. 2234, 82nd Congress 2nd Session (1952) p. 14.

APPENDIX.

STATUTES INVOLVED.

Section 64a of the Bankruptcy Act (52 Stat. 874, 11 U. S. C. §104a).

104. (§64) DEBTS WHICH HAVE PRIORITY—a. The debts to have priority, in advance of the payment of dividends to creditors, and to be paid in full out of bankrupt estates, and the order of payment, shall be (1) the actual and necessary costs and expenses of preserving the estate subsequent to filing the petition; the filing fees paid by creditors in involuntary cases; where property of the bankrupt, transferred or concealed by him either before or after the filing of the petition, shall have been recovered for the benefit of the estate of the bankrupt by the efforts and at the cost and expense of one or more creditors, the reasonable costs and expenses of such recovery; the costs and expenses of administration, including the trustee's expenses in opposing the bankrupt's discharge, the fees and mileage payable to witnesses as now or hereafter provided by the laws of the United States, and one reasonable attorney's fee, for the professional services actually rendered, irrespective of the number of attorneys employed, to the petitioning creditors in involuntary cases and to the bankrupt in voluntary and involuntary cases, as the court may allow; (2) wages, not to exceed $600 to each claimant, which have been earned within three months before the date of the commencement of the proceeding, due to workmen, servants, clerks or traveling or city salesmen on salary or commission basis, whole or part time, whether or not selling exclusively for the bankrupt; (3) where the confirmation of an arrangement or wage earner plan or the bankrupt's discharge has been refused, revoked, or set aside upon the objection and through the efforts and at the cost and expense of one or more creditors, or, where through the efforts

and at the cost and expense of one or more creditors, evidence shall have been adduced resulting in the conviction of any person of an offense under this Act, the reasonable costs and expenses of such creditors in obtaining such refusal, revocation, or setting aside, or in adducing such evidence; (4) taxes legally due and owing by the bankrupt to the United States or any State or any subdivision thereof: Provided, That no order shall be made for the payment of a tax assessed against any property of the bankrupt in excess of the value of the interest of the bankrupt estate therein as determined by the court: And provided further, That, in case any question arises as to the amount or legality of any taxes, such question shall be heard and determined by the court; and (5) debts owing to any person, including the United States, who by the laws of the United States in [is] entitled to priority, and rent owing to a landlord who is entitled to priority by applicable State law; Provided, however, That such priority for rent to a landlord shall be restricted to the rent which is legally due and owing for the actual use and occupancy of the premises affected, and which accrued within three months before the date of bankruptcy.

Section 67b and c of the Bankruptcy Act (52 Stat. 875 (1938); 11 U. S. C. §107b and c).

107. (§67) LIENS AND FRAUDULENT TRANSFERS. —b. The provisions of section 60 of this Act [§96 of this title] to the contrary notwithstanding, statutory liens in favor of employees, contractors, mechanics, landlords, or other classes of persons, and statutory liens for taxes and debts owing to the United States or any State or subdivision thereof, created or recognized by the laws of the United States or of any State, may be valid against the trustee, even though arising or perfected while the debtor is insolvent and within four months prior to the filing of the

petition in bankruptcy or of the original petition under chapter 10, 11, 12, or 13 of this Act [§§501 to 1086 of this title], by or against him. Where by such laws such liens are required to be perfected and arise but are not perfected before bankruptcy, they may nevertheless be valid, if perfected within the time permitted by and in accordance with the requirements of such laws, except that if such laws require the liens to be perfected by the seizure of property, they shall instead be perfected by filing notice thereof with the court.

c. Where not enforced by sale before the filing of a petition in bankruptcy or of an original petition under chapter 10, 11, 12, or 13 of this Act [§§501 to 1086 of this title], though valid under subdivision b of this section, statutory liens, including liens for taxes or debts owing to the United States or to any State or subdivision thereof, on personal property not accompanied by possession of such property, and liens whether statutory or not, of distress for rent shall be postponed in payment to the debts specified in clauses (1) and (2) of subdivision a of section 64 of this Act [§104 of this title], and, except as against other liens, such liens for wages or for rent shall be restricted in the amount of their payment to the same extent as provided for wages and rent respectively in subdivision a of section 64 of this Act [§104 of this title].

UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT

No. 11,793

In the Matter of
QUAKER CITY UNIFORM CO., INC.,
Bankrupt.
DANIEL P. VELORIC,
Appellant.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF PENNSYLVANIA.

Argued March 6, 1956
Before GOODRICH, KALODNER AND STALEY, *Circuit Judges.*

OPINION OF THE COURT

(Filed July 27, 1956)

By STALEY, *Circuit Judge.*

This appeal involves the distribution of certain funds in the hands of the trustee in bankruptcy for the Quaker City Uniform Co., Inc., of Philadelphia, Pennsylvania, which was adjudged a bankrupt on July 2, 1953, by the Dis-

trict Court for the Eastern District of Pennsylvania. Specifically, we are asked to determine what should be the relative order of distribution among (1) chattel mortgage holders prior in time to any claimants, (2) the landlord of the bankrupt who had made a distraint for rent but not sold any property, (3) various wage claimants, and (4) administration expenses.

At the time of bankruptcy, two chattel mortgagees, Daniel P. Veloric, appellant here, and Fidelity-Philadelphia Trust Company, had valid liens under Pennsylvania law upon certain goods in the bankrupt's possession. The bankrupt's landlord, Delsea Corporation, also held a valid lien under Pennsylvania law upon all goods on the bankrupt's premises for rent due. In addition to these liens, claims were asserted against the bankrupt's estate by various assignees of wage claimants (Philadelphia Joint Board, Amalgamated Clothing Workers of America; College Hall Fashions; and Synthetic Specialists, Inc.) and by the trustee for administration expenses.

The bankrupt's goods were sold by the trustee with an understanding between counsel for the trustee and chattel mortgagee Veloric that funds realized from the sale would be substituted for the pledged goods.

The referee in bankruptcy concluded that the order of distribution should be—first, the chattel mortgagees because their liens were not affected by the adjudication in bankruptcy; second, the administration costs; third, the wage claims; and fourth, the landlord's claim. According to the referee, the administration costs and wage claims were put ahead of the landlord's claim because of Section 67(c) of the Bankruptcy Act.

The district court agreed with the referee that the chattel mortgagees were entitled to payment ahead of the administration costs and wage claims but ordered that the landlord be paid out of the amount awarded to the chattel mortgagees because, under the law of Pennsylvania, interests of the chattel mortgagees were subjected to the landlord's lien.

We cannot concur in either the referee's or the district court's order of distribution of the fund. For the reasons which follow, the order of distribution shall be (1) administration expenses, (2) wage claims, (3) landlord's claim, (4) claims of the chattel mortgagees.

Subsection (c) of Section 67 of the Bankruptcy Act reads in part:

> "(c) Where not enforced by sale before the filing of a petition initiating a proceeding under this act, and except where the estate of the bankrupt is solvent: (1) though valid against the trustee under subdivision (b) of this section, statutory liens, including liens for taxes or debts owing to the United States or to any State or any subdivision thereof, on personal property not accompanied by possession of such property, and liens, whether statutory or not, of distress for rent shall be postponed in payment to the debts specified in clauses (1) and (2) of subdivision (a) of section 64 of this act and such liens for wages or for rent shall be restricted in the amount of their payment to the same extent as provided for wages and rent respectively in subdivision (a) of section 64 of this act * * *." 52 Stat. 877 (1938), as amended 66 Stat. 427 (1952), 11 U.S.C. §107(c) (1952 ed.).

Under this section, debts which are specified in clauses (1) and (2) of subdivision (a) of Section 64[1] are entitled to payment ahead of statutory liens on personal property not accompanied by possession and liens, whether statutory or not, of distress for rent.

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[1] "64. Debts which have priority.

"(a) The debts to have priority, in advance of the payment of dividends to creditors, and to be paid in full out of bankrupt estates, and the order of payment, shall be (1) [subdivision (1) contains a list of proper items for payment in connection with administration]; (2) wages, not to exceed $600 to each claimant, which have been earned within three months before the date of the commencement of the proceeding, due to workmen, servants, clerks, or traveling or city salesmen on salary or commission basis, whole or part time, whether or not selling exclusively for the bankrupt * * *." 52 Stat. 874 (1938), as amended 66 Stat. 426 (1952), 11 U.S.C. §104(a) (1952 ed.).

The claims in this case for administration expenses and for wages are the claims specified in clauses one and two of Section 64(a), and thus they are entitled to payment before the satisfaction of liens mentioned in Section 67(c).

Both the referee and the district court concluded that, because of Section 67(c), the satisfaction of the landlord's lien was to be postponed in payment to the claim for administration expenses and the claims for wages. This was clearly correct under the section. But that section not only postpones the landlord's lien; it also postpones the liens of the chattel mortgagees, and we cannot agree with the assumption which apparently has guided the parties in this appeal that the liens of the chattel mortgagees are not postponed. The liens of the chattel mortgagees in this case fit exactly the type of liens that are postponed in payment by Section 67(c). They are statutory liens under Pennsylvania law; they are on personal property and were not accompanied by possession. That the reference to statutory liens in Section 67(c) (which was introduced by the Chandler Act of 1938) was intended to apply to all statutory liens on personal property not accompanied by possession seems clear from the explanatory analysis of that section in a Committee Report Analysis of H.R. 12889, 74th Cong., 2d Sess. (1936), which said:

> "Section 64 is declaratory of a policy that the costs and expenses in connection with a bankruptcy proceeding and its administration shall be first paid in distribution. It is a sound policy and is in accordance with the general principles well established in liquidation proceedings. But Section 67 of the Act does not apply the same limitation with respect to valid liens. The Supreme Court, in the case of City of Richmond v. Bird, 43 A.B.R. 260 (1919), resolved the conflict in the lower court decisions by holding that the priority provisions of Section 64 do not apply to liens valid under Section 67. The Fifth Circuit in the recent case of City of Dallas v. Ryan, 22 A.B.R. (N.S.) 378 (1933),

following the law laid down in the Bird case, held that the priority provisions of Section 64 apply only to general unsecured claims, after the payment of specific liens and encumbrances; and that established liens obtained before bankruptcy and not invalidated by bankruptcy are not affected by that section.

"It is significant that in recent years state legislatures have been enacting special legislation in favor of tax claims, public debts, and a variety of private claims. Statistics in the bankruptcy cases show that the effective administration of the bankruptcy law has seriously suffered therefrom. Such claims, particularly tax liens, often consume the entire estate, leaving nothing for the payment of the costs and expenses of administration incurred in reducing the assets to cash. In many such cases the tax liens represent an accumulation of delinquent items covering a long period of time, without any attempt on the part of tax collectors to enforce payment prior to the bankruptcy proceeding.

"There is therefore need for a provision to protect the administration costs and expenses; and similar considerations apply to wage claims. Accordingly we have selected, from among the priorities fixed by Section 64 (as revised), these particular items for protection. However, by reason of the historical development and the inherent differences existing in the incidents attaching to real and personal property, it would seem advisable to restrict the remedy thus provided to liens on personal property, where such liens have not been enforced by sale prior to bankruptcy."[2]

4 Collier on Bankruptcy 287 et seq. supports the view we have taken as to the meaning of Section 67(c).

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[2] The §67(c) provisions apparently originated in amendments proposed in the 74th Congress. The section finally enacted by the 75th Congress was substantially the same. See Goggin v. Division of Labor Law Enforcement of California, 336 U.S. 118, note 8 (1949).

Under that section, then, the claim for administration expenses and the claims for wages have priority over the claims of the landlord and the chattel mortgagees. As between the administration expenses and the wages, the administration expenses are given priority by Section 64(a). As between the landlord and the chattel mortgagees, the landlord is entitled to priority. This is so because, except in situations where federal law has spoken, priority among liens is determined by the law of the state, 4 Collier on Bankruptcy 1347; Id. 1955 Cum. Supp. and cases cited therein, and admittedly under Pennsylvania law the landlord's lien by way of distraint takes precedence over a chattel mortgage even though the landlord's levy is subsequent in time to the recordation of the mortgage.

Thus, out of the funds in the trustee's hands, first the administration expenses should be paid in full; second, the wage claimants should be paid to the extent that they are entitled to a priority under Section 64, third, the landlord should be paid in full; and fourth, the chattel mortgagees should be paid. Some other questions raised by the parties need not be considered.

For the foregoing reasons the order of the district court will be reversed and the cause remanded with instructions to proceed in accordance with this opinion.

A true Copy:

Teste:

Clerk of the United States Court of Appeals for the Third Circuit.

UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT

No. 11,793

In the Matter of
QUAKER CITY UNIFORM CO., INC.,
Bankrupt.
DANIEL P. VELORIC,
Appellant.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF PENNSYLVANIA.

Reargued October 2, 1956
Before GOODRICH, KALODNER AND STALEY, *Circuit Judges.*

OPINION OF THE COURT

(Filed October 31, 1956)

By STALEY, *Circuit Judge.*

This appeal involves the distribution of certain funds in the hands of the trustee in bankruptcy for the Quaker City Uniform Co., Inc., of Philadelphia, Pennsylvania, which was adjudged a bankrupt on July 2, 1953, by the Dis-

trict Court for the Eastern District of Pennsylvania. Specifically, we are asked to determine the relative order of distribution among (1) chattel mortgage holders prior in time to any claimants, (2) the landlord of the bankrupt who had made a distraint for rent but who had not sold any property, (3) various wage claimants, and (4) administration expenses.

The facts are stipulated. The bankrupt leased premises for its business from the Delsea Corporation, the landlord. The bankrupt gave a chattel mortgage to one Veloric on August 30, 1951, and a second chattel mortgage to Fidelity-Philadelphia Trust Company on August 19, 1952. Both mortgages were duly recorded on their respective days of delivery. Non-payment of rent prompted the Delsea Corporation to issue a landlord's warrant on May 12, 1953. The constable levied on all the goods on the bankrupt's premises, including the goods securing both chattel mortgages. The sale of the goods under the distraint was stayed by execution issued by the sheriff. On June 16, 1953, an involuntary petition in bankruptcy was filed. The following claims were asserted against the fund of $9,896.77 in the hands of the trustee:[1]

1. Administration expenses	$ 676.00
2. Philadelphia Joint Board, Amalgamated Clothing Workers of America, valid wage claims	2,543.53
3. College Hall Fashions, assignees of valid wage claims	1,517.00
4. Synthetic Specialists, Inc., assignees of valid wage claims	7,001.60
5. Delsea Corporation, landlord; gross rent in arrears	3,641.07
6. Veloric, chattel mortgagee	3,480.00

[1] An agreement was reached between counsel that the mortgaged chattels be sold and the amount realized from the sale substituted for the pledged personalty. The proceeds of that agreed sale represent the bulk of the funds in the hands of the trustee.

7. Fidelity-Philadelphia Trust Company, chattel mortgagee 2,612.80

Section 64 of the Bankruptcy Act (11 U.S.C.A. §104) provides priorities among certain *unsecured* creditors. This section does not purport to dictate priorities among holders of valid liens. In fact, it is only after valid liens are satisfied that Section 64 becomes operative.

The Chandler Act of 1938 introduced Section 67, sub. c (11 U.S.C.A. §107, sub. c):

> "c. Where not enforced by sale before the filing of a petition initiating a proceeding under this Act * * * (1) though valid against the trustee under subdivision (b) of this section, statutory liens * * * on personal property not accompanied by possession of such property, and liens, whether statutory or not, of distress for rent shall be postponed in payment to the debts specified in clauses (1) and (2) of subdivision (a) of section 64 of this Act * * *."

Thus expenses of administration and wage claims, while normally merely unsecured claims given first and second priority as such under Section 64, sub. a, become payable under the specific language of Section 67, sub. c, before the lien of the landlord.

Except in situations where federal law has spoken, priority among liens is determined by the law of the state. Seymour v. Wildgen, 137 F. 2d 160, 161 (C.A. 10, 1943); 4 Collier on Bankruptcy 296, 1347 (14th ed.) By settled Pennsylvania law, the landlord's lien by way of distraint takes precedence over a chattel mortgage, and this notwithstanding the fact that the landlord's levy was subsequent in time to the recordation of the mortgage. Commercial Credit Plan v. Mahoney, 67 Pa. D.&C. 577 (1948); see also Reinhart v. Gerhardt, 152 Pa. Super. 229 (1943); National Cash Register Co. v. Ansell, 125 Pa. Super. 309 (1937). The wage claim assignees are not lien-holders, and their claims must be predicated upon their status as

unsecured creditors entitled to second priority under Section 64, sub. a, of the Bankruptcy Act.[2] Applicable Pennsylvania lien law would thus give the landlord's lien priority over the lien of the chattel mortgage; the claim for wages would come last. And such would be the order of distribution for these items if Section 67, sub. c, were inapplicable. The state lien law applies, of course, only where federal law has not supplanted it.

As we have seen, Section 67, sub. c, expressly subordinated the lien of the landlord to the payment of administrative expenses and wage claims, the first and second priorities under Section 64, sub. a. The referee took the position that since the landlord's lien was subordinated under Section 67, sub. c, and the liens of the chattel mortgages were not so postponed expressly by the section, these latter liens were to be satisfied first; then administrative expenses and wage claims were to be paid, and finally the landlord's lien. Such also was the position taken by the chattel mortgagees. The district court agreed with the referee that the chattel mortgagees were entitled to payment ahead of administration costs and wage claims but ordered that the landlord be paid out of the amount awarded to the chattel mortgagees because, under the law of Pennsylvania, interests of the chattel mortgagees were subjected to the landlord's lien. In the Matter of Quaker City Uniform Co., Inc., 134 F. Supp. 596 (E.D.Pa. 1955).

The intent of Congress in the passage of Section 67, sub. c, as stated in 4 Collier on Bankruptcy 288 (14th ed.), was "to provide a measure of much-needed protection, (1)

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[2] See In re Curran's Restaurant & Baking Co., 11 F. Supp. 8, 9 (E.D. Pa. 1934), where it was decided that the Pennsylvania statute (43 Purdon's Pa. Stat. Annot. §221) did not give wage claimants a "lien" cognizable in bankruptcy even though the word "lien" was used in the statute. And even if the statute meant that a "lien" was given, there is nothing in the record of the instant case to show that such wage claims were filed in the appropriate prothonotary's office as required by the Act. In the case of In re Pennsylvania Central Brewing Co., 114 F. 2d 1010, 1012 (C.A. 3, 1940), cert. denied 312 U.S. 685 (1941), failure to file wage claims as prescribed by statute was deemed sufficient to deny the claim the status of a lien.

for administrative costs and expenses in the interest of bankruptcy administration, and (2) for wage claims in the interest of protecting a weak but deserving economic class, against the ravages of certain accumulated liens on the bankrupt's property." Again, the purpose of subordination of liens was expressed in a Committee Report Analysis of H.R. 12889, 74th Cong., 2d Sess. (1936) 212, n. 1:

> "There is therefore need for a provision to protect the administration costs and expenses; and similar considerations apply to wage claims. Accordingly we have selected, from among the priorities fixed by Section 64 (as revised), these particular items for protection."[3]

We are in agreement with the opinion of the district court that Congress did not intend by Section 67, sub. c, to disturb the priority of liens established by state law. Its sole concern was apparently to insure payment of administrative expenses and small wage claims. See California State Dept. of Employment v. United States, 210 F. 2d 242, 244 (C.A. 9, 1954). However, we are unable to agree with the reasoning of the district court which would save the landlord's lien from subordination because of the existence of a chattel mortgage.

It is not necessary to decide whether or not a Pennsylvania chattel mortgage is a "statutory lien" within the meaning of Section 67, sub. c, and thus subordinated by that section to administration expenses and wage claims.[4] For the purposes of this opinion, however, we shall *assume*

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[3] Cited in Goggin v. California Division of Labor, 336 U.S. 118, 127-128 note 8 (1949).

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[4] Clause (2) of Section 67, sub. c, states that "statutory liens created or recognized by the laws of any State for debts owing to any person * * * shall not be valid against the trustee * * *." The effective date of this amendment was October 7, 1952. Since both chattel mortgages in the instant case were recorded before that date, the amendment, prospective only in its effect, is not applicable here.

that it is not a "statutory lien" within the purview of Section 67.[5] Thus the determinative issue may be stated in this manner: Where a landlord's lien which is subordinated by Section 67, sub. c, is superior under applicable lien law to the lien of a chattel mortgage not within the express terms of Section 67, sub. c, is this latter lien also subordinated by necessary implication?[6] We are of the opinion that it is.

There are a few cases which suggest solutions to this problem. In City of New Orleans v. Harrell, 134 F. 2d 399 (C.A. 5, 1943), involving a dispute between a chattel mortgagee and the City which claimed a superior tax lien, the court held the tax lien ineffectual because it had not been properly perfected. There is, however, in that opinion dictum to the effect that even if the tax lien had been perfected, the chattel mortgage would be paid first because its lien is unaffected by bankruptcy, whereas Section 67, sub. c, expressly subordinates tax liens to the priorities of administration expenses and wage claims.

This was the position of the referee in the case at bar. It must be noted, however, that such an interpretation would ascribe to Congress the intent that a chattel mortgagee should benefit from the event of bankruptcy, before which his lien was inferior to the landlord and after which it became the superior lien. This view contains the undesirable feature of needlessly upsetting state lien priority rules, and for that reason it was expressly rejected in California

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[5] In re Tele-Tone Radio Corp., 133 F. Supp. 739 (D.C.N.J. 1955), decided that a factor's lien in New Jersey was not a "statutory lien" within Section 67, sub. c.

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[6] This problem of priority in lien circuity has been described as "insoluble on any known principles" (Andrus v. Burke, 61 N.J. Eq. 297, 299 (Ch. 1901), 48 Atl. 228, 229, and a "first-rate legal puzzle" (in Professor Kocourek's article in 29 Ill. L. Rev. 952, 1935). Osborne, Mortgages (1951) 532-539 summarizes seven methods of solution in these problems of lien circuity. However, it must be remembered that the intent of Congress must be given operative effect in bankruptcy proceedings, and consequently we are given little assistance by decided cases which do not touch federal questions.

State Dept. of Employment v. United States, 210 F. 2d 242, 244 (C.A. 9, 1954):

> "From a consideration of both the language used in the Act and the legislative history we are persuaded that §67, sub. c does not affect or impair the priorities of liens * * *."

The last mentioned case suggests the following solution. Enough from the estate should be set aside to satisfy the holder of the lien superior by applicable lien law. However, since this superior lien is subordinated under Section 67, sub. c, from the amount thus set aside must be paid expenses of administration and wage claims. Whatever remains goes to the holder of the inferior lien. The difficulty presented by this solution is that the superior lien will be defeated to the extent of the administrative expenses and wage claims. (See 4 Collier on Bankruptcy 299 n. 43.) This criticism is forcefully apposite in the factual situation presented here. The wage claims asserted in this case would consume the entire amount set aside for the landlord, and even worse than the fear of merely upsetting state lien priority, the application of the rule in this case would completely *destroy* the superior state lien.

A further review of possible solutions would not aid in the determination of the issue presented here.

In view of the fact that Congressional intent was to favor expenses of administration and wage claims while leaving state priorities unaffected, we hold that the lien of the chattel mortgage, inferior under state law, is by necessary implication postponed by Section 67, sub. c, to a position behind the subordinated landlord's lien.[7] Thus, the

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[7] Note 14 in 4 Colliers on Bankruptcy 291 discussed Section 67, sub. c: "While clause (1) of subdivision c is restricted in its terms to statutory liens and liens of distress for rent, other liens not within its terms may be subordinated under an interpretation that liens inferior under applicable lien law to those postponed by §67c(1) are likewise postponed by necessary implication."

Footnote 41 at page 297 is explanatory of this result: "This mode of disposition carries out the view that the subordination provision does not affect

order of payment becomes: (1) costs of administration (2) wage claimants; (3) landlord; and (4) chattel mortgagees. Since the administration expenses and wage claims will consume the bankrupt's estate, nothing will remain for the landlord or the chattel mortgagees; it follows that the limitation in the amount of the payment to the landlord under Section 67, sub. c, need not be discussed.

The order of the district court will be reversed and the cause remanded with directions to proceed in conformity with this opinion.

A true Copy:

Teste:

Clerk of the United States Court of Appeals for the Third Circuit.

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the relative priority of [landlord] and [chattel mortgagee], and that the subordination of [chattel mortgagee] as well as [landlord] to the claims entitled to priority under §64a is merely the incidental result of the application of §67c(1) to [landlord's] lien. It presumably underlies Matter of Michael's Cafeteria, Inc. (D.La. 1943), 53 Am.B.R. (N.S.) 289, 49 F. Supp. 657, **on rehearing** 55 Am.B.R. (N.S.) 332, 52 F. Supp. 799, where the court apparently subordinated a chattel mortgage along with a prior landlord's lien to administrative and wage claims."

54/13

FILED

JAN 2 8 1957

JOHN T. FEY, Clerk

IN THE

Supreme Court of the United States

Term, 1957.

No. 717

In the Matter of
QUAKER CITY BUSHORE CO., INC., Bankrupt.

DANIEL P. VELOSKI and FIDELITY-PHILADELPHIA TRUST COMPANY,

Appellees,

and

COLLEGE HALL FASHIONS and STRETCH-SPECIALISTS, INC.,

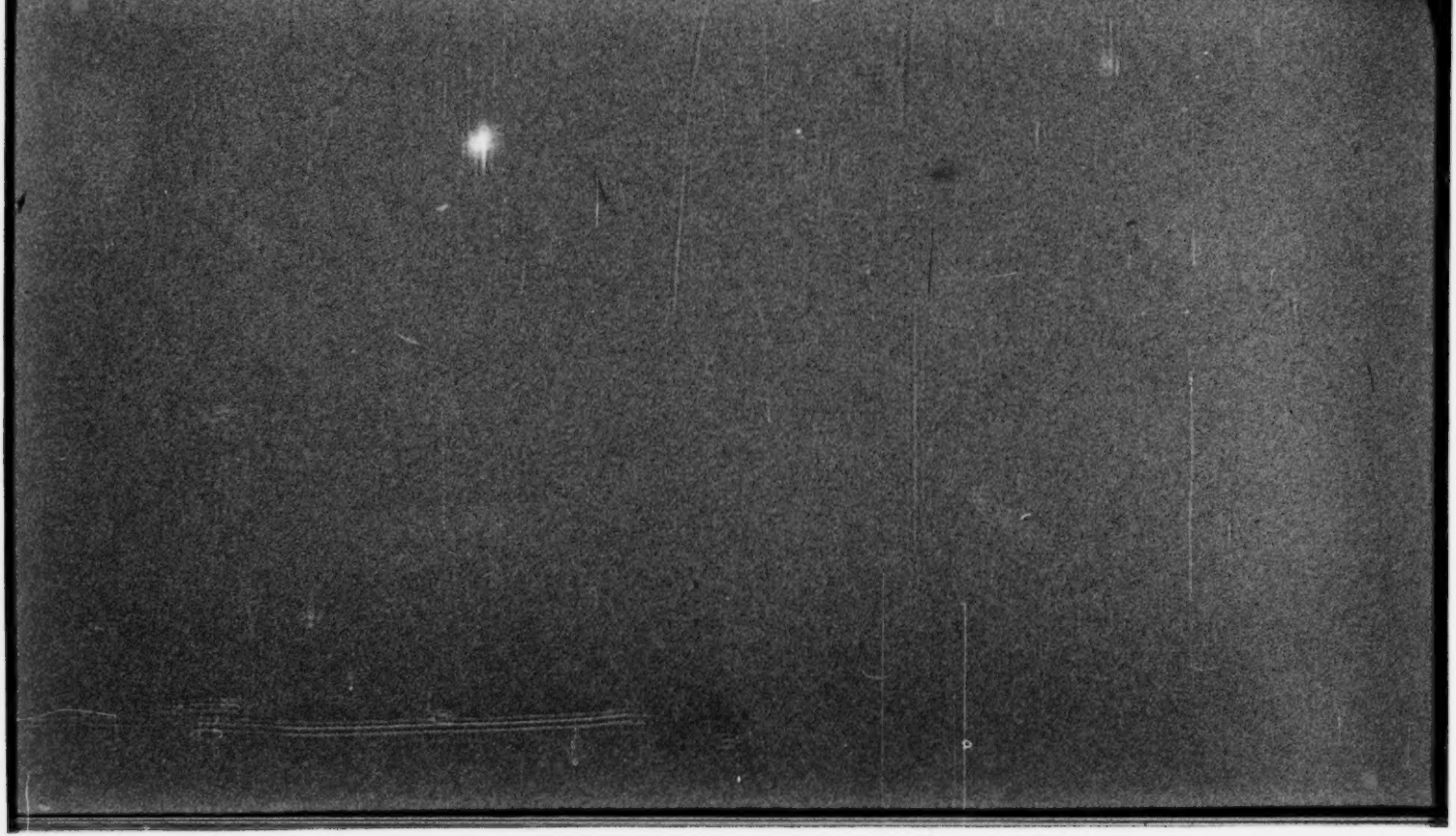
Respondent,

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

John E. Mussina,
Morton M. Wexler,
Wexler, Mussina & Wiesenthal,
909 Market St. Natural Bank Bldg.,
Philadelphia 7, Pa.
Attorneys for Daniel P. Veloski.

William M. Kunzman,
James Alan Montgomery, Jr.,
Pepper, Bodine, Stern, Simmons
& Hamilton,
900 Fidelity-Phila. Trust Bldg.,
Philadelphia 9, Pa.
Attorneys for Fidelity-Phila. Tr. Co.

Intercontinental, 156 Chestnut St., Phila. 6, Pa.



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IN THE

Supreme Court of the United States.

Term, 1957.

No. .

IN THE MATTER OF:

QUAKER CITY UNIFORM CO., INC., BANKRUPT.

DANIEL P. VELORIC AND FIDELITY-PHILADELPHIA TRUST COMPANY,

Petitioners,

AND

COLLEGE HALL FASHIONS AND SYNTHETIC SPECIALISTS, INC.,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

Daniel P. Veloric and Fidelity-Philadelphia Trust Company, a corporation of the Commonwealth of Pennsylvania, petitioners, pray that a Writ of Certiorari issue to review the judgment of the United States Court of Appeals for the Third Circuit, entered in the above-entitled case on October 31, 1956.

I. CITATIONS TO OPINIONS BELOW.

The opinion of the Referee in Bankruptcy (R. p. 14a) is unreported and is printed in appendix hereto, *infra*, p. 20.

The opinion of the District Court (R. p. 24a) printed in the appendix hereto, p. 29 is reported in 134 F. Supp. 596.

The first opinion of the United States Court of Appeals for the Third Circuit (R. p. 28a) was filed on July 27, 1956, and is unofficially reported in 135 of The Philadelphia Legal Intelligencer No. 25, p. 1, column 3, and is printed in appendix hereto *infra*, p. 32. Following the granting of a timely Petition for Reargument that opinion was withdrawn and on October 31, 1956, a second opinion was filed (R. p. 89a), printed in appendix hereto *infra*, p. 39 and is reported in 238 F. 2d 155, 3rd Cir. 1956.

II. JURISDICTION.

The judgment of the United States Court of Appeals was entered on October 31, 1956 (R. p. 97a), and is printed in appendix hereto *infra*, p. 46. The jurisdiction of this Court is invoked under 28 U. S. C. Section 47c.

III. QUESTIONS PRESENTED.

1. Was it the intention of Congress by Section 67(c) of the Chandler Act to divert the proceeds arising from the sale of mortgaged chattels to the payment of administration expenses and wage claims before applying them in satisfaction of the debt for which the mortgage was given as security?

2. Where state law subordinates the lien of a chattel mortgage to the lien of a landlord's distraint, and under Section 67(c) of the Chandler Act the lien of a landlord's distraint is postponed in payment to both administration

expenses and wage claims, is the lien of the chattel mortgage also postponed in payment to administration expenses and wage claims?

3. Did Congress by Section 67(c) of the Chandler Act, which relates to statutory liens and landlord's distraints, intend to impair or destroy the security of validly existing non-statutory liens including chattel mortgages?

4. Where in the administration of a bankrupt's estate there is a conflict between state law and federal law, should federal law not govern?

IV. STATUTE INVOLVED.

The statutory provisions involved are Sections 60, 64, 67 and 70 of the Bankruptcy Act, 49 Stat. 11 U. S. C., paragraphs 96, 104, 107 and 110. Sections 64(a) and 67(b) and (c) are printed in appendix *infra*, pp. 17; 19.

V. STATEMENT.

The following facts are digested from those found by the Referee and those stipulated by the parties (R. pp. 4a to 13a):

1. An involuntary petition in bankruptcy was filed against Quaker City Uniform Company on June 16, 1953. The jurisdiction of the United States District Court was invoked because the case arose under the Federal Bankruptcy Act.

2. Prior to and at the time of bankruptcy, the bankrupt occupied as tenant premises in Philadelphia owned by the Delsea Corporation.

3. On August 30, 1951 and at the time of bankruptcy the bankrupt was the owner of certain machinery and equipment which were at its place of business above mentioned.

4. On August 30, 1951, bankrupt executed and delivered to Veloric a chattel mortgage on some of that equipment. The mortgage was duly filed of record on the same day. The validity of this mortgage under Pennsylvania and bankruptcy law is admitted.

5. On August 19, 1952, bankrupt executed and delivered to Fidelity-Philadelphia Trust Company a chattel mortgage on some of its equipment. Such mortgage was duly filed of record on the same day. The validity of this mortgage under Pennsylvania and bankruptcy law is admitted.

6. Some of the articles covered by the Fidelity-Philadelphia mortgage were also included in the Veloric mortgage. The Veloric mortgage was thus a first mortgage on all the property covered by it, while the Fidelity-Philadelphia mortgage was a first mortgage as to some and a second mortgage as to other property which it covered.

7. On May 12, 1953, the landlord made a distraint on all the goods of the bankrupt that were on his, the landlord's, premises. The sale under the distraint was stayed under Pennsylvania law because execution was later issued by the sheriff on another debt of the bankrupt. Before the sheriff's sale was held, the bankruptcy petition was filed. The validity of the landlord's statutory lien is admitted.

8. On June 16, 1953, the date of the bankruptcy petition, $3,155.00 was due Veloric under his mortgage, $2,366.40 was due Fidelity-Philadelphia under its mortgage, and the landlord's distraint was for the sum of $3,641.07.

9. Before the bankrupt's assets were sold, Veloric filed a petition for reclamation, and the landlord intervened. It was agreed between Veloric and the receiver in bankruptcy, with the landlord and Fidelity-Philadelphia acquiescing, that the property covered by the chattel mortgages be sold at the receiver's sale, with the fund realized therefrom being substituted for the pledged goods.

10. The chattels pledged under the Veloric mortgage alone realized the sum of $5,515.00.

11. The entire proceeds from the receiver's sale amounted to $9,896.77 (R. p. 15a).

12. Bankrupt also owed various wage claims of which $11,062.13 accrued within three months prior to the filing of the bankruptcy petition.

13. Administration expenses were allowed in the amount of $676.00 by the referee in bankruptcy (R. p. 15a).

14. In the hearing before the referee, the parties stipulated the facts (R. pp. 4a to 13a).

The referee found a conflict between the law of Pennsylvania (under which the landlord was entitled to priority over the chattel mortgagees) and federal law (under which the mortgagees were superior to all other claimants). He held that federal law prevailed. The referee, applying Section 67(c) (11 U. S. C. Sec. 107(c)) (1952 ed.) of the Bankruptcy Law, placed the landlord after costs of administration and wage claims. His order of priority thus was:

(1) Chattel mortgages

(2) Costs of administration

(3) Wage claims

(4) Landlord

The referee, moreover, held that the liens of the chattel mortgagees were neither disturbed nor affected by the bankruptcy and that when the chattels were sold by the Receiver, the liens of the mortgages attached to the fund. He specifically decided that since the chattel mortgages were valid liens they were not affected by the provisions of Sections 64 and 67 of the Bankruptcy Act but, on the contrary, the mortgages were pledges that had to be paid in full before any part of the proceeds could be paid to the bankrupt's estate.

15. The matter having been certified for review, the United States District Court for the Eastern District of Pennsylvania held that the proceeds from the sale of the pledged assets did not constitute a part of the bankrupt's estate, that the mortgagees under bankruptcy law were entitled to this fund, but by virtue of the priority accorded to the landlord by state law, the mortgagees were legally obligated out of their fund to pay the landlord. In effect, therefore, the order of priority of the District Court was as follows:

(1) Landlord

(2) Chattel mortgages

(3) Costs of administration

(4) Wage claims

16. On appeal the United States Court of Appeals for the Third Circuit found that the chattel mortgages were, like the landlord's lien, "statutory liens" under Section 67(c) of the Bankruptcy Act and, therefore, postponed in payment under that section to costs of administration and wage claims. The issue of whether the chattel mortgages were statutory liens had not been argued at any time in the case. The Court in its order fixed the order of priority as follows:

(1) Costs of administration

(2) Wage claims

(3) Landlord

(4) Chattel mortgages

In relegating the chattel mortgagees to fourth position the Court of Appeals held:

(a) That chattel mortgages are statutory liens within the meaning of Section 67(c) of the Bankruptcy Act.

(b) That under Section 67(c) and Section 64 of the Bankruptcy Act administration expenses and wage

claims have priority over the claims of the landlord and the chattel mortgagees.

(c) That under Section 64(a) of the Bankruptcy Act administration expenses are given priority over wage claims.

(d) That under Pennsylvania law the lien of a distraining landlord is given priority over the lien of a chattel mortgagee.

17. A petition for reargument was filed and subsequently reargument was ordered. At the reargument, in addition to the briefs of the parties, four briefs *amici curiae* were also filed, all in opposition to the previous finding of the Court of Appeals that a chattel mortgage is a statutory lien and, therefore, postponed to costs of administration and wage claims under Section 67(c) of the Bankruptcy Act.

After reargument the Court ordered its former opinion withdrawn and its former judgment vacated. It then filed a second opinion from which it deleted its earlier finding that a chattel mortgage was a statutory lien within the meaning of the Bankruptcy Act. But in spite of this the Circuit Court reaffirmed that the order of priority should be the same as it had previously decided. This time the Circuit Court *assumed* that a chattel mortgage is *not* a statutory lien. But it held that since under state law the landlord was prior to the mortgages and under Bankruptcy law the landlord was postponed to administration expenses and wage claims, it followed *by implication* that the chattel mortgages were also postponed. In entering its final judgment on October 31, 1956 the Court of Appeals again fixed the order of priority as follows:

(1) Costs of administration

(2) Wage claims

(3) Landlord

(4) Chattel mortgages

VI. REASONS FOR GRANTING THE WRIT.

Petitioners assign four reasons why the Writ of Certiorari should be granted. *First* the issue is of tremendous importance both legally and economically and in the administration of bankrupt estates. *Secondly,* its adverse effect on the business of making secured commercial loans is critical. *Thirdly,* it creates a conflict in principle with a case in the Fifth Circuit, and *fourthly,* it defeats both the over-all purpose of the Bankruptcy Act and the intention of Congress. The reasons will be briefly discussed in the order stated:

A. The Issue Is of Tremendous Importance Both Legally and Economically.

It has always been considered basic and established law that contractual liens, valid under both state and federal law, are entitled to priority of payment over costs of administration and wage claims in bankruptcy. It was so set forth in Section 67(d) of the Bankruptcy Act prior to 1938 and eliminated at that time only because it was deemed unnecessary to retain it. *4 Collier on Bankruptcy,* page 1344. The law was so well established that, prior to the decision in the instant case, it was seldom, if ever, questioned judicially. On the faith that the law was as stated, billions of dollars have been loaned in secured transactions. In many of these the only security given was a chattel mortgage which, when properly recorded, became a lien on the chattels which it covered. It was believed that this lien was good while the borrower was solvent and continued so if he became a bankrupt. If, by the mortgagor going into bankruptcy, a chattel mortgage could be reduced in the order of priority from first place to fourth place, it is inconceivable that any lender would accept such worthless paper. It would be equally true of other types of commercial paper used in secured transactions such as factor's liens, conditional sales contracts, bailment leases, trust receipts, and security interests under the Uniform Commercial Code.

The rude awakening that a chattel mortgage could be subordinated at all was on July 27, 1956 when the Court of Appeals filed its first opinion in the instant case. This decision was highlighted by the lower court's unprecedented pronouncement that chattel mortgages were statutory liens within the meaning of Section 67(c) of the Chandler Act. Having thus reduced the consensual or contractual liens to the status of statutory liens, it was not difficult for the lower court to subordinate the chattel mortgages to administration expenses, wage claims and the landlord's distraint. But it is most difficult to see how the lower court was able to reach the same result, after assuming, as it did, in its second opinion, that the chattel mortgages were not statutory liens within the meaning of Section 67(c) of the Chandler Act. Certainly there had been no change in the law, either statutory or decisional, that warranted such an upheaval in judicial decision.

Petitioners submit that the importance of the issue both legally and economically commends itself as a sufficient reason for granting the Writ prayed for.

B. The Adverse Effect of the Lower Court's Decision on the Commercial World Is Critical.

The impact of the first decision of the Court of Appeals in the case at Bar was felt immediately. This is abundantly demonstrated by the fact that when a petition for reargument was filed four briefs *amici curiae* were filed in addition to the briefs of the parties. These included briefs *amici curiae* that were filed on behalf of seven large banks and the National Commercial Finance Conference, Inc. by recognized authorities in the field of secured transactions and bankruptcy. Their intervention was prompted by their sharing the two-fold interest of petitioners. They wanted the holding that a chattel mortgage was a statutory lien withdrawn and they wanted the integrity of a chattel mortgage as a first lien preserved in bankruptcy. It was generally recognized that if the first of their objectives was achieved, the second would inevitably follow. Such,

however, was not the case. On the contrary, in its second opinion the Court of Appeals reaffirmed its subordination of the chattel mortgages to fourth position of priority even though it recalled its earlier pronouncement that the chattel mortgages were statutory liens. The fact that the integrity of a chattel mortgage as a first lien is still in jeopardy where the mortgagor's bankruptcy ensues is a matter of vital and deep concern to the entire commercial world and equally so in the administration of bankrupt estates.

The impact of the case becomes more serious because of the frequency with which it will be felt and the varied circumstances under which it will recur.

The instant case involves a landlord's lien which is given priority over chattel mortgages under the law of Pennsylvania. Under Section 67(c) of the Chandler Act it is postponed in payment to costs of administration and wage claims. The decision of the Court of Appeals relegates the chattel mortgages, otherwise entitled to first order of priority, to fourth position behind the landlord.

This case cannot, however, be regarded as an isolated one. Similar situations arise with frequency in Pennsylvania where state law accords priority to landlords over chattel mortgages and other forms of security on personalty under the Uniform Commercial Code, as well as in all other states according landlords priority over chattel mortgages, conditional sales, factors' liens, trust receipts, etc.

The impact of the case will also be widespread since it will not be restricted to cases involving a landlord's lien. That is only one of the many statutory liens given favored treatment by Section 67(b) of the Chandler Act. Numerous other liens are accorded similar treatment. Most important are state and local taxes. These are frequently given priority over chattel mortgages and other liens on personalty by local law. There are also liens for taxes owing to the United States, statutory liens in favor of employees, contracts, mechanics, landlords and other classes of persons.

It is submitted by petitioners that the decision of the Court of Appeals rendered in the instant case will be serious and critical when applied to the many cases that will involve both a contractual lien, a landlord's lien, and a statutory lien of the classes above enumerated and even unliened priority claims under Section 64(a)(5) of the Chandler Act. In all of these situations, if the instant case remains authoritative, contrary to established law and business practice, secured claims on personalty will be relegated to a position after administration costs, wage claims and statutory liens and even unliened priorities under Section 64(a)(5) in the Third Circuit and all circuits following it.

Secondly, the adverse impact of the holding in the administration of bankruptcy estates has already been felt and the holding has already been extended. In the Referee's unreported opinion (United States District Court for the Eastern District of Pennsylvania), in *Re George Townsend Co., Inc.,* decided November 23, 1956 (reprinted in the appendix *infra,* p. 47), the conflict arose between a landlord, tax claims, both liened and unliened, a chattel mortgagee and a conditional sales vendor. The latter two had secured interests admittedly valid, which prior to the instant case, would have been entitled to first order of priority.

The landlord had not distrained and therefore had no lien on the goods pledged under the chattel mortgage and conditional sale. He had at most a priority claim under Section 64(a)(5) of the Bankruptcy Act (entitled to payment after costs of administration, wage claims and liened tax claims). The Referee felt that the instant case compelled the result that under state law the landlord's claim, though not a lien, was entitled to priority over the secured interests, and ordered distribution in the following order:

(1) Costs of administration
(2) Wage claims (there were none)
(3) Federal tax lien
(4) Landlord
(5) Conditional sale and chattel mortgage

It is significant that in both the instant case and the *Townsend* case the funds were insufficient to pay lien claimants and priority claims in full. The result is that in both cases, the secured claimants, with claims valid under both state and federal law, and prior to the instant case entitled to first order of priority, now find themselves relegated to fourth and fifth places, which means they receive nothing. It is apparent that the critical impact of the instant case has already been felt in other cases.

C. The Decision in the Instant Case Conflicts in Principle With a Case in the Fifth Circuit.

The decision in the instant case is in conflict in principle with the decision of the United States Court of Appeals for the Fifth Circuit in *City of New Orleans v. Harrell*, 134 F. 2d 399 (1943). In that case a chattel mortgage was given first order of payment. A municipal tax lien was relegated to a position after costs of administration and wage claims pursuant to Section 67(c) of the Bankruptcy Act. Had the tax lien been perfected under local law (or by notice under Section 67(c)), it would have had priority under local law, but nevertheless would have been postponed under Section 67(c), just as in the instant case. Both the majority opinion and the concurring opinion of Judge Hutcheson held that the chattel mortgage still would have been entitled to first order of priority, over costs of administration, wage claims and the tax lien. This is in conformity with established law and business practice. On the contrary, in the instant case both chattel mortgages are relegated to a position after costs of administration, wage claims and the landlord's lien.

Petitioners contend that the conflict between the decisions rendered in the case at Bar and the *City of New Orleans v. Harrell* case is inescapable if judged in the light of the facts and results. The conflict was admittedly more direct under the first opinion of the Court of Appeals in the

instant case. In writing its second opinion the Court studiously avoided any pronouncement that a chattel mortgage is a statutory lien. A reading of the two cases is persuasive that if the case at Bar were to be decided by the Court of Appeals for the Fifth Circuit the chattel mortgages would be given first priority in the order of payment. Petitioners regard this as a compelling reason why the Writ of Certiorari should be granted as prayed for.

D. The Decision in the Instant Case Defeats the Purpose of the Bankruptcy Act and the Intention of Congress.

Under Section 70(a) of the Bankruptcy Act (11 U. S. C. 110) the Trustee in Bankruptcy succeeded to the bankrupt's title to the chattels. The title acquired was subject to the two mortgage liens of petitioners. These mortgages were valid under Pennsylvania law because they were filed as required by the Act of June 1, 1945, P. L. 1358, 21 Purd. St. 940.

The liens of petitioners' mortgages were not disturbed nor affected by the filing of the petition in bankruptcy (Section 70(a) of the Bankruptcy Act). When the chattels were sold by the Receiver in Bankruptcy the liens of the mortgages attached to the proceeds of sale. *R. F. C. v. Cohen,* 179 F. 2d 773, 10th Cir. 1950. *Lockhart v. Garden City Bank,* 116 F. 2d 658, 2 Cir. 1940.

It is the contention of petitioners, as decided by the Referee in Bankruptcy, that the chattel mortgages are valid liens and were not affected by Sections 64 and 67 of the Bankruptcy Act but are secured interests that must be paid before the bankrupt estate can receive the balance, if any, *Richetts v. First Trust, etc.,* 73 F. 2d 599, 8th Cir., 1934.

It is manifestly clear from a reading of the Bankruptcy Act that contractual or consensual liens valid under state law were to be so recognized and treated in the administration of a bankrupt's estate.

By Section 67(c) of the Chandler Act Congress provided long sought and much needed relief to the estates of bankrupts that were being impoverished and consumed by large landlord's and tax liens at the expense of administration expenses and wage claims. That it was this evil that Congress sought to correct is clear from a reading of Report No. 1409 of the House of Representatives of the 75th Congress, first session, which with respect to Section 64 of the Chandler Act reads as follows at pages 15 and 16:

> "(4) Priorities—Section 64: * * * All state priorities have been deleted except in the case of a landlord, but that priority is restricted to rent for actual use and occupancy which accrued within 3 months before bankruptcy. Under the laws of many states a landlord is granted either a priority or a lien for rent. Many leases contain a clause permitting the acceleration of rent for an unexpired term. Therefore, landlords frequently present claims for rent for unexpired terms and obtain priority under their state laws. The statistics gathered by the Attorney General indicate that rent claims consume a very substantial portion of an estate, and in smaller estates not infrequently use up all of the funds. In some jurisdictions where the rent has become a lien without the necessity of distraint before bankruptcy, the claim takes priority over all administration costs including the costs of preserving the estate. Such a situation is inequitable. In Section 67(c) a similar provision is made to cover the claims of landlords which by state law are made liens, as distinguished from priorities."

Petitioners submit that it was never the intention of Congress to take mortgaged assets or their proceeds from the mortgagee and use them to pay administration costs and wages.

The Court of Appeals concedes that Section 67(c) of the Chandler Act which expressly postpones the payment

of a landlord's distraint to the payment of administration costs and wages does not expressly postpone a chattel mortgage. It follows that if Section 67(c) were strictly construed, the chattel mortgages would not be postponed.

But the Court of Appeals holds that the chattel mortgages are postponed under Section 67(c) *by implication.* The Court thus ascribes to Congress an intention to do something drastic by implication that it could easily have done by express terms had it so intended.

As a matter of law it is urged that an error of great importance was committed by the Court of Appeals in its interpretation of the law. It applied the principle that when federal law has not spoken, state law controls. It found that federal law had not spoken. We believe this is error.

Briefly the situation is as follows:

(a) Under state law, a landlord's lien, though subsequent in time, prevails over a prior chattel mortgage (conditional sale, bailment lease, factor's lien, trust receipt or security interest under the Uniform Commercial Code). Here state law has spoken.

(b) Section 67(b) of the Bankruptcy Act protects statutory liens, including a landlord's distraint, which would otherwise be vulnerable as voidable preferences under Section 60 of the Bankruptcy Act. But Section 67(c) then explicitly postpones such statutory liens to costs of administration and wage claims. Significantly it does not postpone non-statutory liens such as a chattel mortgage, which is contractual and consensual. Here federal law has spoken.

(c) The chattel mortgages are admittedly valid liens under both state and Bankruptcy law and admittedly normally entitled to first order of priority of payment under Bankruptcy law. The Bankruptcy Act does not postpone chattel mortgages. Thus, they remain first in order of priority under Bankruptcy law.

(d) Thus, where federal law has explicitly postponed landlords' liens and has not postponed chattel mortgages or other consensual liens, it seems that here the Court of Appeals fell into error, first, by not recognizing that federal law had spoken and, secondly, by not following and applying it.

VII. CONCLUSION.

It is the contention of petitioners that both of the decisions of the Court of Appeals rendered in this case are erroneous. But it is also their contention that the later of these decisions which still stands is of such vast importance that it should be reviewed by the Supreme Court of the United States. Altogether there have been four decisions rendered, one by the Referee, another by the District Court and two by the Court of Appeals. Successively, the Referee was reversed by the District Court and the latter was in turn reversed by the Court of Appeals. These different decisions have resulted in chaos and uncertainty which have been detrimental to business, industry, banking and the law.

To alleviate this condition and to clarify the law, it is earnestly submitted by petitioners that the Writ of Certiorari should be granted by your Honorable Court as prayed for.

Respectfully submitted,

JOHN E. MULDER,
MORRIS M. WEXLER,
WEXLER, MULDER & WEISMAN,
Attorneys for Daniel P. Veloric.

WILLIAM M. KEENAN,
JAMES ALAN MONTGOMERY, JR.,
PEPPER, BODINE, FRICK, SCHEETZ & HAMILTON,
Attorneys for Fidelity-Philadelphia Trust Company.

VIII. APPENDIX.

Section 64 Subsection a of the Bankruptcy Act.

(52 Stat. 874, 11 U. S. C. § 104(a).)

The debts to have priority, in advance of the payment of dividends to creditors, and to be paid in full out of bankrupt estates, and the order of payment, shall be (1) the actual and necessary costs and expenses of preserving the estate subsequent to filing the petition; the fees for the referees' salary fund and for the referees' expense fund; the filing fees paid by creditors in involuntary cases or by persons other than the bankrupts in voluntary cases; where property of the bankrupt, transferred or concealed by him either before or after the filing of the petition, shall have been recovered for the benefit of the estate of the bankrupt by the efforts and at the cost and expense of one or more creditors, the reasonable costs and expenses of such recovery; the costs and expenses of administration, including the trustee's expenses in opposing the bankrupt's discharge or in connection with the criminal prosecution of an offense punishable under chapter 9 of Title 18, or an offense concerning the business or property of the bankrupt punishable under other laws, Federal or State; the fees and mileage payable to witnesses as now or hereafter provided by the laws of the United States, and one reasonable attorney's fee, for the professional services actually rendered, irrespective of the number of attorneys employed, to the petitioning creditors in involuntary cases and to the bankrupt in voluntary and involuntary cases, as the court may allow: *Provided, however,* That where an order is entered in a proceeding under any chapter of this title directing that bankruptcy be proceeded with, the costs and expenses of administration incurred in the ensuing bankruptcy proceeding

shall have priority in advance of payment of the unpaid costs and expenses of administration, including the allowances provided for in such chapter, incurred in the superseded proceeding and in the suspended bankruptcy proceeding, if any; (2) wages not to exceed $600 to each claimant, which have been earned within three months before the date of the commencement of the proceeding, due to workmen, servants, clerks, or traveling or city salesmen on salary or commission basis, whole or part time, whether or not selling exclusively for the bankrupt; (3) where the confirmation of an arrangement or wage-earner plan or the bankrupt's discharge has been refused, revoked, or set aside upon the objection and through the efforts and at the cost and expense of one or more creditors, or, where through the efforts and at the cost and expense of one or more creditors, evidence shall have been adduced resulting in the conviction of any person of an offense under chapter 9 of Title 18, the reasonable costs and expenses of such creditors in obtaining such refusal, revocation, or setting aside, or in adducing such evidence; (4) taxes legally due and owing by the bankrupt to the United States or any State or any subdivision thereof: *Provided,* That no order shall be made for the payment of a tax assessed against any property of the bankrupt in excess of the value of the interest of the bankrupt estate therein as determined by the court: *And provided further,* That, in case any question arises as to the amount or legality of any taxes, such question shall be heard and determined by the court; and (5) debts owing to any person, including the United States, who by the laws of the United States is entitled to priority, and rent owing to a landlord who is entitled to priority by applicable State law: *Provided, however,* That such priority for rent to a landlord shall be restricted to the rent which is legally due and owing for the actual use and occupancy of the premises affected, and which accrued within three months before the date of bankruptcy.

Section 67 Subsection b of the Bankruptcy Act.
(52 Stat. 875 (1938), 11 U. S. C. § 107(b).)

"The provisions of Section 60 of this Act to the contrary notwithstanding, statutory liens in favor of employees, contractors, mechanics, landlords, or other classes of persons, and statutory liens for taxes and debts owing to the United States or any State or subdivision thereof, created or recognized by the laws of the United States or any State, may be valid against the trustee, even though arising or perfected while the debtor is insolvent or within 4 months prior to the filing of the petition in bankruptcy by or against him. Where by such laws such liens are required to be perfected and arise but are not perfected before bankruptcy, they may nevertheless be valid, if perfected within the time permitted by and in accordance with the requirements of such laws, except that if such laws require the liens to be perfected by the seizure of property, they shall instead be perfected by filing notice thereof with the court."

Section 67 Subsection c of the Bankruptcy Act.
(52 Stat. 875 (1938), 11 U. S. C. § 107(c).)

"c Where not enforced by sale before the filing of a petition initiating a proceeding under this act, and except where the estate of the bankrupt is solvent: (1) though valid against the trustee under subdivision (b) of this section, statutory liens, including liens for taxes or debts owing to the United States or to any State or any subdivision thereof, on personal property not accompanied by possession of such property, and liens, whether statutory or not, of distress for rent shall be postponed in payment to the debts specified in clauses (1) and (2) of subdivision (a) of section 64 of this act and such liens for wages or for rent shall be restricted in the amount of their payment to the same extent as provided for wages and rent respectively in subdivision (a) of section 64 of this act * * *. 52 Stat. 877 (1938), as amended 66 Stat. 427 (1952), 11 U. S. C. § 107(c) (1952 ed.)."

IN THE
UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

IN BANKRUPTCY.

CAUSE NO. 23857.

IN THE MATTER OF
QUAKER CITY UNIFORM COMPANY, INC.,
Bankrupt.

Opinion and Order of the Referee Sur Lien Claims and Priority Claims.

STATEMENT OF CASE.

This controversy arises out of the various claims interposed to a fund in the hands of the trustee in bankruptcy, and the Referee is to determine the relative order of distribution under the Bankruptcy Act.

All material facts have been stipulated by the various claimants and the same is incorporated herein by reference, made part hereof as if the same were repeated verbatim and are the Referee's findings of facts, with one correction to be noted in Paragraph 12 of the stipulation wherein the amount realized from the sale should be $5515.00, instead of $4515.00, and two additional findings set forth in the last two paragraphs of this statement of the case.

The various claimants are as follows:

1. Daniel P. Veloric, chattel mortgagee holders, pp. 3, 4, 6, 8, 9, 11 and 12 of stipulation of facts, amount of claim $3480.00.

2. Fidelity-Philadelphia Trust Company, chattel mortgage holder, pp. 3, 5, 6, 8 and 10 of stipulation of facts; amount of claim $2612.80.

3. Delsea Corporation, landlord, pp. 1, 2, 7, 8, 11, 13, 15, 16 of stipulation of facts, amount of claim $3641.07.

4. Phila. Joint Board, Amalgamated Clothing Workers of America, wage claimants, par. 17 of the stipulation of facts; amount of claim $2543.53.

5. College Hall Fashions, wage claimant, par. 18 of the stipulation of facts; amount of claim $1517.00.

6. Synthetic Specialists, Inc., wage claimant, par. 19 of the stipulation of facts; amount of claim $7001.60.

While paragraph 12 shows the amount realized from the sale as $4515.00 (corrected to read $5515.00), actually this sum represents only the amount subject to the Veloric chattel mortgage, while the total amount of the entire fund is $9896.77 this is a finding of fact made by the Referee, in addition to the stipulation of facts signed by the claimants, rendered necessary by the statement in paragraph 12, relative to the amount of money involved.

Allowance of $676.00 for expenses and fee was made to the counsel for the trustee, but this amount was held up pending determination of the various lien and priority claimants, and payment of this allowance, if valid, would bring the amount in question to $9220.77. It thus becomes apparent that the trustee is the legal holder of the fund involved and that administration expenses and wage claimants are affected by the order of distribution that may be interposed herein, supplemental brief of the landlord to the contrary notwithstanding.

QUESTION INVOLVED.

What relative order of distribution should be made in bankruptcy of a fund in the hands of the trustee therein, between claimants (1 and 2) valid chattel mortgage holders, prior in point of time to any claimants; claimant (3) a landlord who had made a distraint for rent but has not sold the property, and claimants (4, 5, 6) sundry assignees of wage claimants; and sundry costs of administration?

DISCUSSION.

Claimants are in agreement that claimant 1, chattel mortgage holder, is ahead of claimant 2, chattel mortgage holder, and that claimants 4, and 6, the assignees of wage claimants, are to share in the proportion of their claims to the fund involved.

In House Report No. 2320 to S. 2234, 82nd Cong. 2nd Sess. (1952) 13, the following language is to be noted:

> "There is accordingly reason to restrict such liens to the same extent that priorities are restricted. The Chandler Act also adopted the view that a landlord should not be encouraged to accumulate liens of indefinite extent and thus contribute to building up unsound financial positions on the part of tenants to the disadvantage of general creditors, Section 67-c accordingly postponed such liens to administrative expenses and to wages, which to the extent of $600.00 earned within three months of bankruptcy were for the first time given by Section 64-a priority second only to expenses of administration and outranking all other priority claims, including taxes, which were assigned to the fourth degree of priority.
>
> "Wages having thus been given prescribed priority under 64-a, Section 67-c then proceeded to restrict the recognition of liens for wages on personal property unaccompanied by possession to the same extent that

their priority was restricted. Landlord's liens were likewise restricted. It was thought, however, unnecessary to restrict wage or rent claims for the benefit of junior lien holders . . ."

Three cases in this district are partly dispositive of the issue:

In re Goldstein, 34 F.S. 876 9/9/40
In re Jay and Dee, 37 F.S. 989 3/19/41
In re Lebed, 39 F.S. 457, 6/30/41

The entire District Court sat in the Jay and Dee case, supra, and J. Welsh in his opinion said, inter alia,

"that the law be so construed as to give priority to costs and wages where the landlord's lien has not been enforced by a sale prior to bankruptcy."

In the case of In re Lebed, supra, the late Judge Bard said—

"thus while both a lien of distress for rent unenforced by sale, and a priority or charge for rent existing under state law are restricted as to the amount of preference in distribution to rent accrued within three months of bankruptcy, a landlord's lien is postponed in payment only to the claims provided for in Section 64, sub. a".

In one of the latest cases, Rochelle v. McLendon, 5 Cir. 1953 Texas, 208 F. 2nd 442, the court held:

"Damages for anticipatory breach of lease contract, based on loss of unearned future rent, are not entitled to priority. The plain meaning of this is that, where the landlord has not taken possession of the goods and chattels of the bankrupt at the time of bankruptcy, he shall be paid as a lien creditor only to the extent of the rent accrued and unpaid within three months prior to bankruptcy."

Accordingly, in the light of the foregoing cases the Referee is of the opinion that the wage claims and sundry administration expenses are to be paid before the landlord.

It must be conceded that the two mortgagees held valid and subsisting mortgages on June 16, 1953, when the petition in bankruptcy was filed. Veloric's mortgage had been a first lien against the chattels, which it covered since August 30th, 1951, when it was duly filed. Fidelity-Philadelphia Trust Company's mortgage, duly filed August 19th, 1952, became a second lien as to the chattels which its mortgage covered along with the Veloric mortgage, and with respect to additional assets not covered by the Veloric chattel mortgage, the Fidelity-Philadelphia mortgage was a first lien.

The Chattel Mortgage Act of June 1, 1945, P.L. 1358, 21 Purd. St. 940 provides—

> "Any chattel mortgage executed pursuant to this Act shall be a lien upon the property therein described, which lien shall be good and valid against and superior to all rights of subsequent purchasers, subsequent mortgagees and other subsequent lienors and encumbrancers, and all persons subsequently dealing with the mortgaged property or subsequently acquiring an interest therein from the time of the filing of the mortgage."

The bankrupt corporation gave and executed the mortgages as the holder of legal title and it retained the same legal title and possession of the chattels up until June 16, 1953, when the petition in bankruptcy was filed.

As a result of this petition the trustee in bankruptcy succeeded to the bankrupt's title and possession. The liens of the mortgages, however, were not disturbed, nor affected by the banktruptcy (Section 70-A) and when the chattels were sold by the receiver the liens of the mortgages attached to the fund.

R.F.C. v. Cohen, 10 Cir. 1950, 179 F(2), 773:

"The holder of a valid lien upon property belonging to the estate of a bankrupt does not waive any of his rights by coming into a pending bankruptcy proceeding."

Lockhart v. Garden City Bank, 116 F(2), 658:

"Liens good at time of filing of petition in bankruptcy do not lose their validity as against bankruptcy trustee unless statute so expressly provides."

Since the chattel mortgages are valid liens they are not affected by the provisions of Sections 64 and 67, but are pledges that must be paid before the bankrupt estate can receive the balance or equity remaining therein. In Richetts v. First Trust, etc., 73 F. 599, the Court, at page 602, said:

"the trustee was not bound to accept whatever property interest the bankrupt may have had in these securities, because the duties to be performed and the expenses to be advanced in connection therewith rendered the property onerous and unprofitable."

Also in re Stroudsburg Supply, etc., 248 Fed. 356, where the Court said—

"It is in fact his duty (Trustee's) to redeem such property where the same may be accomplished by the payment of less than its value, so as to realize an equity . . ." (Italics supplied).

The trustee may abandon any property which is either worthless or overburdened, or for any reason certain not to yield any benefit to the general estate.

First National Bank v. Lasatar, 196 U.S. 115
Stanoline Oil & Gas Co. v. Logan, 92 F. 28
R.F.C. v. Cohan, 179 F(2), 773
In re Yalden, 109 F.S. 603

Matter of International Fuel, 3 Cir. 1927, 21 Fed (2) 598—

> "The express right of trustee in bankruptcy under General Order 28, held to carry with it right to use reasonable means for redemption including the borrowing of money per Court order to redeem pledge."

Judge Clary, in the matter of Harry G. Litt, individually and trading as People's Market, Cause No. 23458, decided January 27, 1955, in a somewhat similar case involving a government's tax lien, applied the federal law as set forth in the decision of the Supreme Court in the case of U.S. vs. R. P. Scovill et al, Oct. Term, 1954, No. 35, decided Jan. 10, 1954. The latter court held that a distress lien not perfected in the federal sense as this, is a matter of federal law.

In the case of U.S. v. Gilbert Associates, 345 U.S. 361, the town of Walpole held an ad valorem tax claim on machinery. The Court held that the town was not a judgment creditor, but the holder of a general lien on all the taxpayer's property; that in claims of this type, specificity requires that the lien be attached to certain property by reducing it to possession; that the taxpayer had not been divested by the town of either title or possession, and therefore had only a general imperfected lien.

In U.S. v. Security Trust et al, 34 U.S. 47, the Court held that although a state court's classification of a lien as specific and perfected is entitled to weight, it is subject to reexamination by the Federal Court.

In U.S. v. Waddil, Holland & Flinn, 323 U.S. 353, in a contest between a landlord's lien and municipal tax lien against a federal claim for priority under R.S. 3466, the Court said—

> "but it is a matter of federal law as to whether a lien created by state statute is sufficiently specific and perfected to raise questions as to the applicability of the priority given the claims of the U. S. by an Act of Con-

gress. If the priority of the United States is ever to be displaced by a statutory lien, federal courts must be free to examine the lien's actual legal effect upon the parties. A state court's characterization of a lien as specific and perfected, however conclusive as a matter of state law, cannot operate by itself to impair or supersede a long standing Congressional declaration of priority."

The foregoing cases are cited and quoted in two cases handed down the same day as the Scovil case, supra, i.e. U.S. v. Michael P. Acri et al, No. 33, Oct. Term, 1954, a sixth circuit case involving an attachment lien; and U.S. v. The Liverpool & London & Globe et al, No. 34 Oct. Term, 1954, a 5th Circuit Case involving a lien of garnishment.

It is significant to note the words of the Supreme Court in the Acri case supra—"The state's characterization of its liens, while good for all state perposes, does not necessarily bind this court".

The foregoing review of authorities has been made because the position of the lien claimants and priority claimants must be viewed in the light of the federal law. If the state law were to prevail, under the lower court decisions, which are the only authorities available, the Pennsylvania distribution would be as follows:

1. Landlord
2. Chattel mortgages
3. Wage claims

Smaller War Plants v. McCullough, 52 D & C, 545 Chattel mortgage holder v. wage claimants

Commercial Credit Plan v. Mahoney et al, Chattel mortgage holder v. landlord

Ferbro Trading Corp. v. Jo Mar Dress Co., 78 D & C, 337, chattel mortgage holders v. landlord.

Shepherd's Citation also list 13 Pits L.R. 131
13 Pits L.R. 584
57 D.L.R. 128

Accordingly, the Referee is of the opinion and holds that the chattel mortgages of Veloric and the Fidelity-Philadelphia Trust Company must be first paid out of the fund, together with a reasonable attorney's fee for each claimant, which the Referee sets at $100.00 each for the record counsel representing the chattel mortgage holder. Second to be paid out will be administration expenses, then comes, in order of priority, the assignees of the wage claims and then the landlord. (Since the amount of the wage claims will eat up the balance of the fund, the question of any tax claims becomes academic).

CONCLUSIONS OF LAW.

1. The chattel mortgage of Daniel P. Veloric has the first claim for payment out of the fund in question.

2. The chattel mortgage of Fidelity-Philadelphia Trust Co. has the second claim for payment out of the fund in question.

3. Administration expenses have the third claim for payment out of the fund in question.

4. Assignees of the wage claims have the fourth claim for payment out of the fund in question.

5. Landlord has the fifth claim for payment out of the fund in question.

THOMAS J. CURTIN,
Referee in Bankruptcy.

February 15th, 1955

IN THE
UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

In Bankruptcy

(Filed September 7, 1955)

No. 23857

In the Matter of:

QUAKER CITY UNIFORM COMPANY, INC.
Bankrupt

Opinion of the United States District Court Sur Certificate of Review.

Before KIRKPATRICK, *Ch. J.*

This is a contest in which the trustee in Bankruptcy is not interested. It is between a chattel mortgagee holding a valid lien and a landlord who distrained for rent prior to the bankruptcy but did not sell. By agreement, the mortgaged property was sold and the proceeds substituted. If bankruptcy had not intervened, the controversy could hardly have arisen, because the law of Pennsylvania clearly subjects the interest of the chattel mortgage to the lien of the landlord's levy. The chattel mortgagee concedes as much, but argues that the Bankruptcy Act nullifies the landlord's preferred status as against him. Sections 64(a) (11 U.S.C. 104a) and 67c (11 U.S.C. 107c) of the Act provide that in the distribution of the estate a landlord's lien shall be postponed to costs of administration, wages and taxes, all of which admittedly come after valid liens such as this chattel mortgage. Of course, it can be said properly enough that the Bankruptcy Act governs and that it was within the power of Congress to accomplish the result con-

tended for by the chattel mortgagee, inasmuch as the legal title to the mortgaged chattels remained in the bankrupt at all times, the mortgage under the law of Pennsylvania being in the nature of a pledge rather than a conveyance. Whether Congress did so or intended to do so is the question in this case.

It will be noted that Section 64a of the Bankruptcy Act (11 U.S.C. 104a) establishes priorities in "bankrupt estates". The words "estate" and "bankrupt estates" in the Act mean the "unincumbered assets generally of a bankrupt, properly administerable in bankruptcy, as distinguished from property of the bankrupt dedicated by law to the payment of a particular obligation or upon which there is a specific lien." In re Menzies, 60 F. 2d 1064, 1067. Regardless of where the bare legal title resided, the mortgaged property or in this case its proceeds, to the extent of the mortgagee's lien upon it, was not in any real sense a part of the bankrupt estate.

The question then is, Did Congress, by the Bankruptcy Act, mean to establish priorities in or to deal with property which formed no part of the assets administerable in bankruptcy? The answer clearly appears to be that it did not. Not only can no logical reason be assigned why Congress should undertake to upset state law by changing the relative standing of liens upon property whose disposition can in nowise affect the administration of the bankrupt's estate and in which general creditors have no interest whatever, but any such purpose would be contrary to the general policy of the Bankruptcy Act, which is to recognize property rights conferred by the state law, so far as is compatible with the administration of the bankrupt estate for the benefit of the creditors.

This does not advance the wage claimants in the order of distribution. The Bankruptcy law puts the chattel mortgagee, with his valid lien, ahead of the costs of administration, wage claims and liens for rent but this landlord has a prior lien upon the interest of the chattel mortgagee.

The landlord does not receive priority as to the bankrupt's equity in the chattels (which *is* part of the bankrupt estate). Such part of the landlord's claim, if any, as cannot be satisfied from the amount of the chattel mortgagee's interest must be deferred, in accordance with the Bankruptcy Act, to administration expenses, wage claims, etc.

The decisions of this Court cited by the Referee and relied upon by the chattel mortgagee all dealt with the landlord's claim of priority upon distribution of the bankrupt estate—property administerable in bankruptcy—and do not touch the point upon which this case is decided.

Order accordingly.

Order Sur Certificate of Review.

And Now, this 13th day of October, 1955, upon motion of Jerome L. Markowitz, Esq., Counsel for Delsea Corporation, after notice to all counsel of record of the submission of this Order, it is hereby ordered, adjudged and decreed as follows:

1. The Certificate of Review in the above captioned matter is hereby sustained and the matter is referred back to the Referee with instructions to make distribution of the fund arising from the sale of the mortgaged property in accordance with the directions contained in the Opinion of this Court sur Certificate of Review filed September 7, 1955.

2. Delsea Corporation, Landlord, shall be paid its claim in full of $3641.07 from the proceeds of said mortgaged property, and the balance shall be awarded to Daniel P. Veloric and Fidelity-Philadelphia Trust Company, Mortgagees, on account of their claims.

BY THE COURT,

/s/ Kirkpatrick,
Ch. J.

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 11,793

In the Matter of
QUAKER CITY UNIFORM CO., INC.,
Bankrupt.

DANIEL P. VELORIC,
Appellant.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF PENNSYLVANIA

Argued March 6, 1956

Before GOODRICH, KALODNER and STALEY, *Circuit Judges.*

First Opinion of United States Court of Appeals
(Filed July 27, 1956)

By STALEY, *Circuit Judge.*

This appeal involves the distribution of certain funds in the hands of the trustee in bankruptcy for the Quaker City Uniform Co., Inc., of Philadelphia, Pennsylvania, which was adjudged a bankrupt on July 2, 1953, by the District Court for the Eastern District of Pennsylvania. Specifically, we are asked to determine what should be the relative order of distribution among (1) chattel mortgage holders prior in time to any claimants, (2) the landlord of the bankrupt who had made a distraint for rent but not sold any property, (3) various wage claimants, and (4) administration expenses.

At the time of bankruptcy, two chattel mortgagees, Daniel P. Veloric, appellant here, and Fidelity-Philadelphia Trust Company, had valid liens under Pennsylvania law upon certain goods in the bankrupt's possession. The bankrupt's landlord, Delsea Corporation, also held a valid lien under Pennsylvania law upon all goods on the bankrupt's premises for rent due. In addition to these liens, claims were asserted against the bankrupt's estate by various assignees of wage claimants (Philadelphia Joint Board, Amalgamated Clothing Workers of America; College Hall Fashions; and Synthetic Specialists, Inc.) and by the trustee for administration expenses.

The bankrupt's goods were sold by the trustee with an understanding between counsel for the trustee and chattel mortgagee Veloric that funds realized from the sale would be substituted for the pledged goods.

The referee in bankruptcy concluded that the order of distribution should be—first, the chattel mortgagees because their liens were not affected by the adjudication in bankruptcy; second, the administration costs; third, the wage claims; and fourth, the landlord's claim. According to the referee, the administration costs and wage claims were put ahead of the landlord's claim because of Section 67(c) of the Bankruptcy Act.

The district court agreed with the referee that the chattel mortgagees were entitled to payment ahead of the administration costs and wage claims but ordered that the landlord be paid out of the amount awarded to the chattel mortgagees because, under the law of Pennsylvania, interests of the chattel mortgagees were subjected to the landlord's lien.

We cannot concur in either the referee's or the district court's order of distribution of the fund. For the reasons which follow, the order of distribution shall be (1) administration expenses, (2) wage claims, (3) landlord's claim, (4) claims of the chattel mortgagees.

Subsection (c) of Section 67 of the Bankruptcy Act reads in part:

> "(c) Where not enforced by sale before the filing of a petition initiating a proceeding under this act, and except where the estate of the bankrupt is solvent: (1) though valid against the trustee under subdivision (b) of this section, statutory liens, including liens for taxes or debts owing to the United States or to any State or any subdivision thereof, on personal property not accompanied by possession of such property, and liens, whether statutory or not, of distress for rent shall be postponed in payment to the debts specified in clauses (1) and (2) of subdivision (a) of section 64 of this act and such liens for wages or for rent shall be restricted in the amount of their payment to the same extent as provided for wages and rent respectively in subdivision (a) of section 64 of this act * * *." 52 Stat. 877 (1938), as amended 66 Stat. 427 (1952), 11 U.S.C. § 107(c) (1952 ed.).

Under this section, debts which are specified in clauses (1) and (2) of subdivision (a) of Section 64 [1] are entitled to payment ahead of statutory liens on personal property not accompanied by possession and liens, whether statutory or not, of distress for rent.

The claims in this case for administration expenses and for wages are the claims specified in clauses one and

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1. "64. Debts which have priority.

"(a) The debts to have priority, in advance of the payment of dividends to creditors, and to be paid in full out of bankrupt estates, and the order of payment, shall be (1) [subdivision (1) contains a list of proper items for payment in connection with administration]; (2) wages, not to exceed $600 to each claimant, which have been earned within three months before the date of the commencement of the proceeding, due to workmen, servants, clerks, or traveling or city salesmen on salary or commission basis, whole or part time, whether or not selling exclusively for the bankrupt * * *." 52 Stat. 874 (1938), as amended 66 Stat. 426 (1952), 11 U. S. C. § 104(a) (1952 ed.).

two of Section 64(a), and thus they are entitled to payment before the satisfaction of liens mentioned in Section 67(c).

Both the referee and the district court concluded that, because of Section 67(c), the satisfaction of the landlord's lien was to be postponed in payment to the claim for administration expenses and the claims for wages. This was clearly correct under the section. But that section not only postpones the landlord's lien; it also postpones the liens of the chattel mortgagees, and we cannot agree with the assumption which apparently has guided the parties in this appeal that the liens of the chattel mortgagees are not postponed. The liens of the chattel mortgagees in this case fit exactly the type of liens that are postponed in payment by Section 67(c). They are statutory liens under Pennsylvania law; they are on personal property and were not accompanied by possession. That the reference to statutory liens in Section 67(c) (which was introduced by the Chandler Act of 1938) was intended to apply to all statutory liens on personal property not accompanied by possession seems clear from the explanatory analysis of that section in a Committee Report Analysis of H.R. 12889, 74th Cong., 2d Sess. (1936), which said:

> "Section 64 is declaratory of a policy that the costs and expenses in connection with a bankruptcy proceeding and its administration shall be first paid in distribution. It is a sound policy and is in accordance with the general principles well established in liquidation proceedings. But Section 67 of the Act does not apply the same limitation with respect to valid liens. The Supreme Court in the case of City of Richmond v. Bird, 43 A.B.R. 260 (1919), resolved the conflict in the lower court decisions by holding that the priority provisions of Section 64 do not apply to liens valid under Section 67. The Fifth Circuit in the recent case of City of Dallas v. Ryan, 22 A.B.R. (N.S.) 378 (1933), following the law laid down in the Bird case, held that

the priority provisions of Section 64 apply only to general unsecured claims, after the payment of specific liens and encumbrances; and that established liens obtained before bankruptcy and not invalidated by bankruptcy are not affected by that section.

"It is significant that in recent years state legislatures have been enacting special legislation in favor of tax claims, public debts, and a variety of private claims. Statistics in the bankruptcy cases show that the effective administration of the bankruptcy law has seriously suffered therefrom. Such claims, particularly tax liens, often consume the entire estate, leaving nothing for the payment of the costs and expenses of administration incurred in reducing the assets to cash. In many such cases the tax liens represent an accumulation of delinquent items covering a long period of time, without any attempt on the part of tax collectors to enforce payment prior to the bankruptcy proceeding.

"There is therefore need for a provision to protect the administration costs and expenses; and similar considerations apply to wage claims. Accordingly we have selected, from among the priorities fixed by Section 64 (as revised), these particular items for protection. However, by reason of the historical development and the inherent differences existing in the incidents attaching to real and personal property, it would seem advisable to restrict the remedy thus provided to liens on personal property, where such liens have not been enforced by sale prior to bankruptcy."[2]

4 Collier on Bankruptcy 287 et seq. supports the view we have taken as to the meaning of Section 67(c).

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2. The § 67(c) provisions apparently originated in amendments proposed in the 74th Congress. The section finally enacted by the 75th Congress was substantially the same. See Goggin v. Division of Labor Law Enforcement of California, 336 U. S. 118, note 8 (1949).

Under that section, then, the claim for administration expenses and the claims for wages have priority over the claims of the landlord and the chattel mortgagees. As between the administration expenses and the wages, the administration expenses are given priority by Section 64(a). As between the landlord and the chattel mortgagees, the landlord is entitled to priority. This is so because, except in situations where federal law has spoken, priority among liens is determined by the law of the state, 4 Collier on Bankruptcy 1347; Id. 1955 Cum. Supp. and cases cited therein, and admittedly under Pennsylvania law the landlord's lien by way of distraint takes precedence over a chattel mortgage even though the landlord's levy is subsequent in time to the recordation of the mortgage.

Thus, out of the funds in the trustee's hands, first the administration expenses should be paid in full; second, the wage claimants should be paid to the extent that they are entitled to a priority under Section 64, third, the landlord should be paid in full; and fourth, the chattel mortgagees should be paid. Some other questions raised by the parties need not be considered.

For the foregoing reasons the order of the district court will be reversed and the cause remanded with instructions to proceed in accordance with this opinion.

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 11,793

In the Matter of
QUAKER CITY UNIFORM CO., INC.,
Bankrupt

DANIEL P. VELORIC,
Appellant.

Present: GOODRICH, KALODNER and STALEY, *Circuit Judges.*

Order Withdrawing First Opinion of United States Court of Appeals

AND NOW, to-wit, this 31st day of October, 1956, IT IS HEREBY ORDERED that the opinion heretofore filed in this case July 27, 1956, be and it hereby is withdrawn.

By THE COURT,

STALEY,
Circuit Judge.

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 11,793

In the Matter of
QUAKER CITY UNIFORM CO., INC.,
Bankrupt

DANIEL P. VELORIC,
Appellant.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF PENNSYLVANIA

Reargued October 2, 1956

Before GOODRICH, KALODNER and STALEY, *Circuit Judges*

Second Opinion of the United States Court of Appeals
(Filed October 31, 1956)

By STALEY, *Circuit Judge.*

This appeal involves the distribution of certain funds in the hands of the trustee in bankruptcy for the Quaker City Uniform Co., Inc., of Philadelphia, Pennsylvania, which was adjudged a bankrupt on July 2, 1953, by the District Court for the Eastern District of Pennsylvania. Specifically, we are asked to determine the relative order of distribution among (1) chattel mortgage holders prior in time to any claimants, (2) the landlord of the bankrupt who had made a distraint for rent but who had not sold any property, (3) various wage claimants, and (4) administration expenses.

The facts are stipulated. The bankrupt leased premises for its business from the Delsea Corporation, the landlord. The bankrupt gave a chattel mortgage to one Veloric on August 30, 1951, and a second chattel mortgage to Fidelity-Philadelphia Trust Company on August 19, 1952. Both mortgages were duly recorded on their respective days of delivery. Non-payment of rent prompted the Delsea Corporation to issue a landlord's warrant on May 12, 1953. The constable levied on all the goods on the bankrupt's premises, including the goods securing both chattel mortgages. The sale of the goods under the distraint was stayed by execution issued by the sheriff. On June 16, 1953, an involuntary petition in bankruptcy was filed. The following claims were asserted against the fund of $9,896.77 in the hands of the trustee:[1]

1. Administration expenses	$ 676.00
2. Philadelphia Joint Board, Amalgamated Clothing Workers of America, valid wage claims	2,543.53
3. College Hall Fashions, assignees of valid wage claims	1,517.00
4. Synthetic Specialists, Inc., assignees of valid wage claims	7,001.60
5. Delsea Corporation, landlord, gross rent in arreas	3,641.07
6. Veloric, chattel mortgagee	3,480.00
7. Fidelity-Philadelphia Trust Company, chattel mortgagee	2,612.80

Section 64 of the Bankruptcy Act (11 U.S.C.A. § 104) provides priorities among certain *unsecured* creditors. This section does not purport to dictate priorities among holders

1. An agreement was reached between counsel that the mortgaged chattels be sold and the amount realized from the sale substituted for the pledged personalty. The proceeds of that agreed sale represent the bulk of the funds in the hands of the trustee.

of valid liens. In fact, it is only after valid liens are satisfied that Section 64 becomes operative.

The Chandler Act of 1938 introduced Section 67, sub. c. (11 U.S.C.A. § 107, sub. c):

> "c. Where not enforced by sale before the filing of a petition initiating a proceeding under this Act * * * (1) though valid against the trustee under subdivision (b) of this section, statutory liens * * * on personal property not accompanied by possession of such property, and liens, whether statutory or not, of distress for rent shall be postponed in payment to the debts specified in clauses (1) and (2) of subdivision (a) of section 64 of this Act * * *."

Thus expenses of administration and wage claims, while normally merely unsecured claims given first and second priority as such under Section 64, sub. a, become payable under the specific language of Section 67, sub. c, before the lien of the landlord.

Except in situations where federal law has spoken, priority among liens is determined by the law of the state. Seymour v. Wildgen, 137 F.2d 160, 161 (C.A.10, 1943); 4 Collier on Bankruptcy 296, 1347 (14th ed.) By settled Pennsylvania law, the landlord's lien by way of distraint takes precedence over a chattel mortgage, and this notwithstanding the fact that the landlord's levy was subsequent in time to the recordation of the mortgage. Commercial Credit Plan v. Mahoney, 67 Pa. D.&C. 577 (1948); see also Reinhart v. Gerhardt, 152 Pa. Super. 229 (1943); National Cash Register Co. v. Ansell, 125 Pa. Super. 309 (1937). The wage claim assignees are not lien-holders, and their claims must be predicated upon their status as unsecured creditors entitled to second priority under Section 64, sub. a, of the Bankruptcy Act.[2] ApplicablePennsylvania

2. See In re Curran's Restaurant & Baking Co., 11 F. Supp. 8, 9 (E. D. Pa. 1934), where it was decided that the Pennsylvania statute (43 Purdon's Pa. Stat. Annot. § 221) did not give wage

lien law would thus give the landlord's lien priority over the lien of the chattel mortgage; the claim for wages would come last. And such would be the order of distribution for these items if Section 67, sub. c, were inapplicable. The state lien law applies, of course, only where federal law has not supplanted it.

As we have seen, Section 67, sub. c, expressly subordinated the lien of the landlord to the payment of administrative expenses and wage claims, the first and second priorities under Section 64, sub. a. The referee took the position that since the landlord's lien was subordinated under Section 67, sub. c, and the liens of the chattel mortgages were not so postponed expressly by the section, these latter liens were to be satisfied first; then administrative expenses and wage claims were to be paid, and finally the landlord's lien. Such also was the position taken by the chattel mortgagees. The district court agreed with the referee that the chattel mortgagees were entitld to payment ahead of administration costs and wage claims but ordered that the landlord be paid out of the amount awarded to the chattel mortgagees because, under the law of Pennsylvania, interests of the chattel mortgagees were subjected to the landlord's lien. In the Matter of Quaker City Uniform Co., Inc., 134 F. Supp. 596 (E.D.Pa. 1955).

The intent of Congress in the passage of Section 67, sub. c, as stated in 4 Collier on Bankruptcy 288 (14th ed.), was "to provide a measure of much-needed protection, (1) for administrative costs and expenses in the interest of bankruptcy administration, and (2) for wage claims in the

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claimants a "lien" cognizable in bankruptcy even though the word "lien" was used in the statute. And even if the statute meant that a "lien" was given, there is nothing in the record of the instant case to show that such wage claims were filed in the appropriate prothonotary's office as required by the Act. In the case of In re Pennsylvania Central Brewing Co., 114 F. 2d 1010, 1012 (C. A. 3, 1940), cert. denied 312 U. S. 685 (1941), failure to file wage claims as prescribed by statute was deemed sufficient to deny the claim the status of a lien.

interest of protecting a weak but deserving economic class, against the ravages of certain accumulated liens on the bankrupt's property." Again, the purpose of subordination of liens was expressed in a Committee Report Analysis of H.R. 12889, 74th Cong., 2d Sess. (1936) 212, n. 1:

> "There is therefore need for a provision to protect the administration costs and expenses; and similar considerations apply to wage claims. Accordingly we have selected, from among the priorities fixed by Section 64 (as revised), these particular items for protection."[3]

We are in agreement with the opinion of the district court that Congress did not intend by Section 67, sub. c, to disturb the priority of liens established by state law. Its sole concern was apparently to insure payment of administrative expenses and small wage claims. See California State Dept. of Employment v. United States, 210 F.2d 242, 244 (C.A. 9, 1954). However, we are unable to agree with the reasoning of the district court which would save the landlord's lien from subordination because of the existence of a chattel mortgage.

It is not necessary to decide whether or not a Pennsylvania chattel mortgage is a "statutory lien" within the meaning of Section 67, sub. c, and thus subordinated by that section to administrative expenses and wage claims.[4] For the purposes of this opinion, however, we shall *assume* that it is not a "statutory lien" within the purview of Sec-

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3. Cited in Goggin v. California Division of Labor, 336 U. S. 118, 127-128 note 8 (1949).

4. Clause (2) of Section 67, sub. c, states that "statutory liens created or recognized by the laws of any State for debts owing to any person * * * shall not be valid against the trustee * * *." The effective date of this amendment was October 7, 1952. Since both chattel mortgages in the instant case were recorded before that date, the amendment, prospective only in its effect, is not applicable here.

tion 67.[5] Thus the determinative issue may be stated in this manner: Where a landlord's lien which is subordinated by Section 67, sub. c, is superior under applicable lien law to the lien of a chattel mortgage not within the express terms of Section 67, sub. c, is this latter lien also subordinated by necessary implication?[6] We are of the opinion that it is.

There are a few cases which suggest solutions to this problem. In City of New Orleans v. Harrell, 134 F.2d 399 (C.A.5, 1943), involving a dispute between a chattel mortgagee and the City which claimed a superior tax lien, the court held the tax lien ineffectual because it had not been properly perfected. There is, however, in that opinion dictum to the effect that even if the tax lien had been perfected, the chattel mortgage would be paid first because its lien is unaffected by bankruptcy, whereas Section 67, sub. c, expressly subordinates tax liens to the priorities of administration expenses and wage claims.

This was the position of the referee in the case at bar. It must be noted, however, that such an interpretation would ascribe to Congress the intent that a chattel mortgagee should benefit from the event of bankruptcy, before which his lien was inferior to the landlord and after which it became the superior lien. This view contains the undesirable feature of needlessly upsetting state lien priority rules, and for that reason it was expressly rejected in California

5. In re Tele-Tone Radio Corp., 133 F. Supp. 739 (D. C. N. J. 1955), decided that a factor's lien in New Jersey was not a "statutory lien" within Section 67, sub. c.

6. This problem of priority in lien circuity has been described as "insoluble on any known principles" (Andrus v. Burke, 61 N. J. Eq. 297, 299 (Ch. 1901), 48 Atl. 228, 229, and a "first-rate legal puzzle" (in Professor Kocourek's article in 29 Ill. L. Rev. 952, 1935). Osborne, Mortgages (1951) 532-539 summarizes seven methods of solution in these problems of lien circuity. However, it must be remembered that the intent of Congress must be given operative effect in bankruptcy proceedings, and consequently we are given little assistance by decided cases which do not touch federal questions.

State Dept. of Employment v. United States, 210 F.2d 242, 244 (C.A.9, 1954):

> "From a consideration of both the language used in the Act and the legislative history we are persuaded that § 67, sub. c does not affect or impair the priorities of liens * * *."

The last mentioned case suggests the following solution. Enough from the estate should be set aside to satisfy the holder of the lien superior by applicable lien law. However, since this superior lien is subordinated under Section 67, sub. c, from the amount thus set aside must be paid expenses of administration and wage claims. Whatever remains goes to the holder of the inferior lien. The difficulty presented by this solution is that the superior lien will be defeated to the extent of the administrative expenses and wage claims. (See 4 Collier on Bankruptcy 299 n. 43.) This criticism is forcefully apposite in the factual situation presented here. The wage claims asserted in this case would consume the entire amount set aside for the landlord, and even worse than the fear of merely upsetting state lien priority, the application of the rule in this case would completely *destroy* the superior state lien.

A further review of possible solutions would not aid in the determination of the issue presented here.

In view of the fact that Congressional intent was to favor expenses of administration and wage claims while leaving state priorities unaffected, we hold that the lien of the chattel mortgage, inferior under state law, is by necessary implication postponed by Section 67, sub. c, to a position behind the subordinated landlord's lien.[7] Thus, the

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7. Note 14 in 4 Colliers on Bankruptcy 291 discussed Section 67, sub. c: "While clause (1) of subdivision *c* is restricted in its terms to statutory liens and liens of distress for rent, other liens not within its terms may be subordinated under an interpretation that liens inferior under applicable lien law to those postponed by § 67c(1) are likewise postponed by necessary implication."

Footnote 41 at page 297 is explanatory of this result: "This mode of disposition carries out the view that the subordination

order of payment becomes: (1) costs of administration; (2) wage claimants; (3) landlord; and (4) chattel mortgagees. Since the administration expenses and wage claims will consume the bankrupt's estate, nothing will remain for the landlord or the chattel mortgagees; it follows that the limitation in the amount of the payment to the landlord under Section 67, sub. c, need not be discussed.

The order of the district court will be reversed and the cause remanded with directions to proceed in conformity with this opinion.

Judgment of the United States Court of Appeals

This cause came on to be heard on the record from the United States District Court for the Eastern District of Pennsylvania and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this Court that the Order of said District Court in this case be, and the same is hereby reversed, and the cause remanded with directions to proceed in conformity with the Opinion of this Court. Each party to bear its own costs.

Attest:

IDA O. CRESKOFF
Clerk

October 31, 1956

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provision does not affect the relative priority of [landlord] and [chattel mortgagee], and that the subordination of [chattel mortgagee] as well as [landlord] to the claims entitled to priority under § 64a is merely the incidental result of the application of § 67c(1) to [landlord's] lien. It presumably underlies Matter of Michael's Cafeteria, Inc. (D. La. 1943) 53 Am. B. R. (N. S.) 289, 49 F. Supp. 657, *on rehearing*, 55 Am. B. R. (N. S.) 332, 52 F. Supp. 799, where the court apparently subordinated a chattel mortgage along with a prior landlord's lien to administrative and wage claims."

IN THE
UNITED STATES DISTRICT COURT FOR THE
EASTERN DISTRICT OF PENNSYLVANIA

In Bankruptcy

Cause No. 24446

In the Matter of
GEORGE TOWNSEND CO., INC.
Bankrupt

Opinion of Referee in Bankruptcy Referred to in Petition

By Bertram K. Wolfe, Referee in Bankruptcy.

This matter involves the distribution of certain funds in the hands of the Trustee. Specifically there must be determined the relative order of distribution among (1) security interests, (2) landlord's claim for rent, (3) administration expenses, and (4) taxes.

The facts are not in dispute. The funds in the hands of the Trustee were realized from the sale of the bankrupts' personal property on demised premises at the time of bankruptcy. At that time there existed against part of the assets sold a valid conditional sale agreement dated August 20, 1954, in favor of Hamilton R. Marsh Co. and a valid chattel mortgage agreement in favor of David W. Wachs, Agent, dated August 6, 1954. By stipulation, the Trustee sold all the assets, the respective security interests to be relegated to the fund realized. Secured claims were filed by these interests and the Marsh claim was allowed in the sum of $902.50 and the Wachs claim in the sum of $828.40, without determining at the time the order of priority of

payment. Administration expenses have been allowed aggregating $2,832.55 which sum includes an item of $735. to the landlord for use and occupation of the demised premises by the Receiver and tax claims have been allowed totaling $3,388.66. A landlord's rent claim has been allowed in the sum of $652.50. The fund in the hands of the Trustee is $5,714.92.

The factual situation and the legal problems in the instant matter are very much like those in the matter of *Quaker City Uniform Co. Inc.*, a case decided by the Court of Appeals for this Circuit on October 31, 1956. In the instant matter, however, the landlord had not distrained before the bankruptcy and we have tax claims to deal with but no wage claims. Moreover, one of the tax claims, that of the Director of Internal Revenue, is a tax lien in the sum of $1,674.34 with interest from July 22,1955.[1] Although the facts are different, as indicated, the principle and reasoning in the Quaker City case certainly point to a solution of the problems in this case.

(1) The tax lien was entered in 1955 and the security liens in 1954. These facts eliminate the thought that the tax lien being postponed by Section 67c(1) by implication postpones the security interests because, under the Quaker City case, only a senior lien that is postponed under applicable lien law (the landlord's distraint versus the chattel mortgage) will postpone a junior lien not otherwise postponed by Section 67c(1). And the postponed tax lien is not senior to the security interests in this case under applicable lien law.

(2) Does the fact that the landlord did not distrain before bankruptcy in this case, change the order of distribution as promulgated in the Quaker City case where there was such a distraint? I think it does. It must

1. It is hoped that neither the Referee nor the Trustee will be censored for allowing this interest to run, as it was impossible to order a distribution until the decision in the Quaker City case was handed down.

first be decided whether or not the right of a landlord to distrain is in itself a lien within the meaning of the bankruptcy law which says "and liens, whether statutory or not, of distress for rent shall be postponed." Section 67c(1).[2]

There are cases in Pennsylvania that use the word lien when they refer to the right of priority. See *Bennette Estate v. Sproul*, 42 Fed. 33 (CCA 1930). On the other hand, *In re West Side Paper Co.*, (C. C. A. 3rd Cir.) 20 Am. B. C. 660; 162 Fed. 110; 15 Ann. Cas. 384 says "The right to distrain is a right in the nature of a lien, rather than a lien, until the goods are actually distrained * * * While there is no specific lien, except on the goods actually distrained under the landlords' warrant, all the goods on the premises are to be considered as being under a *quasi* pledge, which gives superiority to the specific lien established by the distraint."

It will be conceded that the Landlord and Tenant statutes of Pennsylvania (1919 P. L. 1029 as amended) prohibit the landlord from distraining after the goods have been taken into the custody of the law by an execution, but the same law preserves to the landlord his priority whether or not a distraint had been made. And this priority is preserved in bankruptcy on the theory that the filing of a petition is an execution. In re *Goldstein*, 46 Am. B. R. (NS) 63; 34 F. Supp. 876 (D. C. Pa. 1940). I am therefore, of the opinion that the landlord had no lien on the bankrupts' goods in the sense that would make applicable Section 67c(1) or (2) but rather a priority which would be asserted in a bankruptcy case as provided by Section 64a(5).

---

2. In view of my opinion that the right to distrain creates no lien but only a priority, it is not necessary to decide whether or not a landlords' lien for rent is statutory or otherwise. If the right is in fact a lien, then whether or not it is statutory is important because if it is statutory it is invalidated under Section 67c(2) not simply postponed. The answer may be found in the Quaker City case inasmuch as there was certainly a lien by distraint and the Court postponed rather than invalidated.

It is well settled in Pennsylvania Law[3] and approved in the Quaker City case that a landlord's claim, whether lien or priority, is ahead of a security interest, i.e., a chattel mortgage, bailment lease or conditional sale in the absence of a landlord's waiver. We are, therefore, met with the situation where a landlord's priority is behind administration expenses, wages and taxes in bankruptcy distribution (Sec. 64a) but under applicable lien law is ahead of security interests which, standing alone, would be paid first before administration expenses, wages, or taxes. We do not want to disturb the state lien law. Shall we, therefore allow the security interests to say where they are and put the landlord's priority ahead of them, pushing administration expenses, wages, and taxes down the line? I think not. Better to allow the landlord's priority to stay where it is under Section 64a(5) and, because of the state lien law, put the security interests behind it. Such an arrangement would conform with the reasoning of the Quaker City case. How better to express it than attempting to paraphrase a sentence or two from that case which might read "where a landlord's priority which is fixed by Section 64a(5) is superior under applicable lien law to the lien of a security interest not within the express terms of Section 64a, this latter lien is subordinated by necessary implication." And again, "In view of the fact that congressional interest was to favor expenses of administration, wage claims and taxes while leaving state priorities unaffected, we hold that the lien of the security interests, inferior under state law is by necessary implication postponed by Section 64a to a position behind the landlord's priority fixed by Section 64a."

Thus the order of distribution in this case will be (1) administration expenses, (2) the Federal tax lien, (3) other taxes, (4) the landlord's priority for rent, (5) the security interests.

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3. *Commercial Credit Plan v. Mahoney*, 67 Pa. D. & C. 577 (1948); see also *Reinhart v. Gerhardt*, 152 Pa. Super. 229 (1943); *National Cash Register Co. v. Ansell*, 125 Pa. Super, 309 (1937).

The fund is sufficient to pay the administration expenses but not the tax claims in full. The rent claim and the security interests will not be reached. Under the circumstances it will not be necessary to determine the order of priority as between the two security interests.

An order of distribution in conformity herewith will be entered in due course and the date of that order will fix the time from which a Certificate of Review may be filed if any party so desires.

BERTRAM K. WOLFE,
Referee in Bankruptcy.

November 23, 1956

FILED
FEB 27 1957
JOHN T. FEY, Clerk

IN THE

Supreme Court of the United States

October Term, 1956.

No. 717.

In the Matter of:
QUAKER CITY UNIFORM CO., INC., *Bankrupt.*

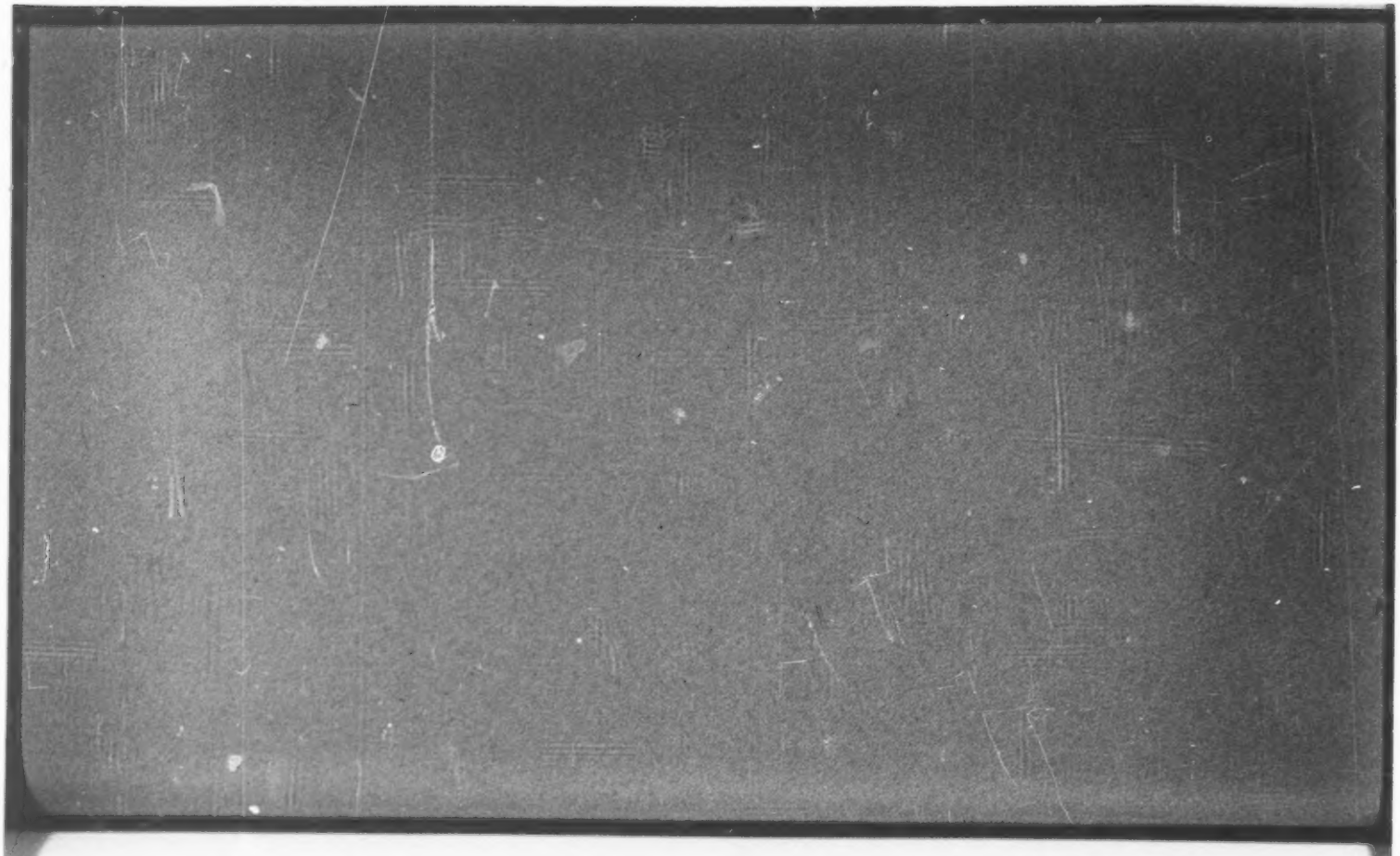
DANIEL P. VELORIC and FIDELITY-PHILADELPHIA TRUST COMPANY,
Petitioners,
and
COLLEGE HALL FASHIONS and SYNTHETIC SPECIALISTS, INC.,
Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

BRIEF FOR RESPONDENTS IN OPPOSITION.

DAVID GOLDBERG,
VERLIN & GOLDBERG,
1011 Finance Building,
Philadelphia 2, Penna.,
Attorneys for Respondents.

Martin & Lyle, 1103 Bankers Securities Bldg., Phila. 7, Pa.



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ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

BRIEF FOR RESPONDENTS IN OPPOSITION.

I. CITATIONS TO OPINIONS BELOW.

The citations to opinions below are as set forth in the petition for a writ of certiorari.

II. JURISDICTION.

Petitioners invoke the jurisdiction of this court under 28 U. S. C., Section 47c.

III. QUESTIONS PRESENTED.

1. Do chattel mortgagees acquire greater rights and priority of payment, as the result of the filing of a petition in bankruptcy, than the rights and priority of payment to which, it is conceded, they are entitled, under state law?

2. Where state law subordinates the lien of a chattel mortgage to the lien of a landlord's distraint, and where such law accords a priority of payment to wage claimants out of the fund arising from the distraint, are the wage claimants entitled to a priority of payment out of the fund realized from the sale of mortgaged chattels upon which the landlord has caused a distraint and levy to be made?

3. Where state law subordinates the lien of a chattel mortgage to the lien of a landlord's distraint, and also subordinates the lien of a landlord's distraint in that it accords priority of payment to wage claimants; and, in addition, under Section 67 (c) of the Chandler Act, the lien of a landlord's distraint is postponed in payment to both administration expenses and wage claims, are the wage claimants entitled to a priority in payment ahead of the landlord and

the chattel mortgagees, when a petition in bankruptcy is filed after a landlord has distrained for rent?

IV. STATUTES INVOLVED.

The statutory provisions involved are as set forth in the petition for a writ of certiorari, and in addition, Section 1 of the Act of Assembly (Pa.) of June 12, 1878, Public Law 207, 43 Purdon's Penna. Statutes 230; and Title and Section 1 of the Chattel Mortgage Act, Act of Assembly (Pa.) of June 1, 1945, Public Law 1358, 21 Purdon's Penna. Statutes 940.1, which Acts are printed in the appendix infra, pp. 15 and 16.

V. STATEMENT.

College Hall Fashions and Synthetic Specialists, Inc., respondents in this action, are the assignees of various wage claimants of Quaker City Uniform Co., Inc., bankrupt. By a stipulation of facts entered into by and between counsel for the receiver, counsel for the petitioners, counsel for the landlord, counsel for the Philadelphia Joint Board, Amalgamated Clothing Workers of America, and counsel for the respondents, it was stipulated and admitted, inter alia, that

> "18. Proof of claim for wages was filed by College Hall Fashions in the amount of $1,517.00, as assignees of a number of wage claims of persons employed by the Bankrupt, which wages were earned within three months of the filing of the petition in bankruptcy, and therefore entitled to priority as such.
>
> 19. Proof of claim for wages was filed by Synthetic Specialists, Inc., in the amount of $7,001.60, as assignee of a number of wage claims of persons employed by the Bankrupt, which wages were earned within three

months of the filing of the petition in bankruptcy, and therefore entitled to priority as such."

Prior to the filing of the petition in bankruptcy, the landlord made a distraint on all the goods of the bankrupt that were on the landlord's premises. The sale under the distraint and levy was stayed under Pennsylvania law because execution was issued by the Sheriff of Philadelphia on another judgment against the bankrupt. Thereafter, the bankruptcy petition was filed before the sheriff's sale was held. The validity of the landlord's distraint and levy is conceded by all of the parties.

By agreement between Veloric, one of the petitioners herein, and the receiver in bankruptcy, the property covered by the chattel mortgages was sold, and the fund realized therefrom was substituted for the mortgaged chattels. The landlord and Fidelity-Philadelphia Trust Company, the other petitioner, acquiesced in this agreement. The respondents were not parties to this agreement.

The proceeds from the receiver's sale of the goods upon all of which the landlord had made a distraint and levy amounted to $9896.77.

The rights and priorities of payment of the various claimants to the fund were then adjudicated by the referee in bankruptcy, United States District Court for the Eastern District of Pennsylvania, and twice by the United States Court of Appeals for the Third Circuit. On two occasions the United States Court of Appeals for the Third Circuit has held that the order of distribution of the funds in the trustee's hands should be: (1) administration expenses; (2) wage claimants; (3) landlord; and (4) chattel mortgagees. It is from this order of distribution that the petitioners pray that a writ of certiorari issue.

VI. ARGUMENT.

A. THE FILING OF A PETITION IN BANKRUPTCY DOES NOT CONFER RIGHTS UPON CHATTEL MORTGAGEES GREATER THAN THOSE CONFERRED UNDER STATE LAW; NOR DOES IT GIVE SUCH MORTGAGEES PRIORITY OF PAYMENT.

The rights, privileges and priority of payment afforded to chattel mortgagees are only those rights which are afforded to them under the applicable state law under which they hold their security. The lien created in favor of chattel mortgagees must arise under the state law. It is recognized in bankruptcy only to the extent of its recognition under the state law. The Bankruptcy Act does not create liens. It only recognizes and gives effect to certain liens which arise out of the state law.

Petitioners have contended throughout this matter that a chattel mortgage is a consensual or contractual lien for the sole reason that it arises out of a contract between the mortgagor and the mortgagee. While this may very well be true in those states which have recognized liens on chattels as part of their common law, it is not true in the State of Pennsylvania, which has consistently refused to recognize or give effect to consensual or contractual liens created on chattels under the common law. In Pennsylvania, chattel mortgages are statutory creations, having been created by the Act of Assembly of June 1, 1945, P. L. 1358, 21 Purdon's Penna. Statutes, 940.1.

The courts of Pennsylvania have consistently held that prior to the passage of the Chattel Mortgage Act, supra, "It had been the settled public policy of the law of this Commonwealth as manifested by legislative acts and judicial decisions, to frown upon the mortgaging of chattels in Pennsylvania"; *First National Bank of Jamestown v. Sheldon*, 161 Pa. Superior Ct. 265; *Roberts' and Pyne's Appeal*, 60 Pa. 400; *Klaus v. Majestic Apartment House Company*, 250 Pa.

194, 95 A. 451; *Kaufmann & Baer v. Monroe Motor Line*, 124 Pa. Superior Ct. 27, 187 A. 296.

Further, it has been repeatedly held under the Pennsylvania common law that it is essential to the validity of a pledge of personal property that either actual or constructive possession of the pledged property be delivered to the pledgees. *Ambler National Bank v. Maryland Credit Finance Co.*, 147 Pa. Superior Ct. 496, p. 502, 24 A. 2d 123.

Since the Chattel Mortgage Act is in derogation of the common law of Pennsylvania, it must be strictly construed, and the rights, duties and remedies of the parties to a chattel mortgage are only as specifically set forth in the statute and may not be inferred. Accordingly, the Pennsylvania courts have consistently held that the common law lien of the landlord is superior to the lien of the chattel mortgagee. Goods in the leased premises are subject to the landlord's distraint when the tenant is in arrears in rent, and it is immaterial that they are held by the tenant under a bailment lease, conditional sale or subject to a chattel mortgage. *Ferbro Trading Corp. v. Jo-Mar Dress Corp., et al.*, 78 Pa. District & County Reports, 337.

In *Commercial Credit Plan v. Mahoney, et al.*, 67 Pa. District & County Reports, 577, it was held that a landlord's distraint for unpaid rent is entitled to a priority over the claim of a chattel mortgagee, *even though the levy of the distraint was made subsequent to the recording of the chattel mortgage.* (Emphasis supplied.)

It has been generally true that the validity and effect of a security agreement are determined by the law of the state in which the chattel is located, at the time the agreement is executed. *In re Industrial Sapphire Manufacturing Co.*, 182 F. 2d 589; *Personal Finance Co. v. General Finance Co.*, 133 Pa. Superior Ct. 582, 3 A. 2d 174; *Restatement Conflict of Laws*, Sections 265, 272, 279.

The District Court and the Court of Appeals both recognized the superior right of the landlord over the chattel mortgagee. In his Opinion, Chief Judge Kirkpatrick stated:

> "If bankruptcy had not intervened, the controversy could hardly have arisen, because the law of Pennsylvania clearly subjects the interest of the chattel mortgage to the lien of the landlord's levy. The chattel mortgagee concedes as much but argues that the Bankruptcy Act nullifies the landlord's preferred status as against him." *In the Matter of Quaker City Uniform Co., Inc., Bankrupt*, 134 F. Supp. 596.

The Learned Chief Judge then fell into error by holding that while the landlord had a priority in the fund over the chattel mortgagees, the wage claimants were not entitled to prior distribution. This ignored the clear provisions of the Pennsylvania law, as well as the provisions of the Bankruptcy Act granting wage claimants priority over rent claims.

The Court of Appeals, in this case, held that except in certain situations, where federal law has spoken, priority among liens is determined by the law of the state, citing *Seymour v. Wildgen*, 137 F. 2d 160; 4 Collier on Bankruptcy, 296, 1347 (14th ed.). The court then held that by settled Pennsylvania law the landlord's lien by way of distraint takes precedence over a chattel mortgage, when the chattel mortgagee has failed to obtain a landlord's waiver. It was the opinion of the court that the interpretation requested by the chattel mortgagees would ascribe to Congress the intent that a chattel mortgagee should benefit from the event of bankruptcy, before which his lien was inferior to the landlord, and after which it became the superior lien. As the court pointed out, this proposition contains the undesirable feature of needlessly upsetting state lien priority rules.

B. THE DECISION BELOW IS CORRECT, AND DOES NOT CONFLICT WITH ANY DECISION OF THIS COURT OR ANY OTHER COURT.

The Court of Appeals concluded that since the Bankruptcy Act does not establish a system of liens, but merely gives effect to the relative standing of liens under applicable state law, it must necessarily follow that under the Pennsylvania law, the lien of the landlord on distraint, is superior to the lien of the chattel mortgagees. The court then applied the clear language of the Chandler Act of 1938, which introduced Section 67, sub. c, 11 U. S. C. A. Section 107, sub. c, the pertinent provisions of which read:

> "c. Where not enforced by sale before the filing of a petition initiating a proceeding under this Act * * * (1) though valid against the trustee under sub-division (b) of this section, statutory liens * * * on personal property not accompanied by possession of such property, and liens, whether statutory or not, of distress for rent shall be postponed in payment to the debts specified in clauses (1) and (2) of subdivision (a) of section 64 of this Act * * *."

The expenses of administration and wage claims, while ordinarily merely unsecured claims given first and second priority as such under Section 64, sub. a, became payable before the lien of the landlord under the specific language quoted above.

The holding of the Court of Appeals is clearly correct under the factual situation in this case. When a Pennsylvania landlord has distrained for rent, and acquired a superior lien over chattel mortgagees, and thereafter bankruptcy intervenes before the sale under the distraint, he is subject to the provisions of the Bankruptcy Act postponing his lien to the payment of administration expenses and wage claims. In such a situation, he may not be paid until after the administration expenses and wage claims are paid to the ex-

tent that they have priority under Section 64 of the Bankruptcy Act. Thereafter, the landlord's claim is to be paid to the extent that he had acquired a lien under applicable Pennsylvania law, and only then may the chattel mortgagees be preferred over other secured and unsecured creditors.

The priority of payment accorded to the wage claimants over the landlord under the Bankruptcy Act, is likewise accorded the wage claimants under Pennsylvania law. The Act of Assembly of June 12, 1878, P. L. 207, Section 1, 43 P. S. 230, provides:

> "It is the true intent and meaning of the provisions of the Act of Assembly, entitled 'An act for the better protection of the wages of mechanics, miners, laborers and others,' passed the 9th day of April, 1872, that the several classes of laborers in said act mentioned shall have a preference over landlords, in all claims for rent * * * where the lessee or lessees are the parties employing the miners, mechanics, laborers or clerks: Provided That any person or persons claiming a preference as above provided, shall give notice of the nature and the amount of his claim to the landlord or his bailiff, before the actual sale of the property levied upon."

Thus, it can be seen that both under the Bankruptcy Act and the applicable Pennsylvania law, the wage claimants have a priority of payment over the landlord.

The decision of the court of appeals does not presume to decide the effect of chattel mortgages in jurisdictions other than Pennsylvania, and in factual situations different from the case at bar. Its decision is manifestly correct under the facts and the law in this case.

Petitioners urge that the instant case conflicts in principle with the decision of the United States Circuit Court of Appeals for the Fifth Circuit, in *City of New Orleans v. Harrell*, 134 F. 2d 399. That case is readily distinguishable from the case at bar. In that case the court held that a tax

lien, which the City of New Orleans claimed was a superior lien, was ineffectual because it had not been properly perfected. The court there reached the conclusion that the City's claim for unpaid taxes was a statutory lien within the meaning of the Bankruptcy Act, and that since it was not accompanied by possession it did not take precedence over a chattel mortgage which had been recorded prior thereto. In the instant case, the landlord's lien had been perfected by the distraint and levy for rent, and his lien was superior to the lien of the chattel mortgagees.

C. THE DECISION BELOW RAISES NO IMPORTANT QUESTION OF FEDERAL LAW.

The Petitioners do not seriously urge that an important question of federal law has been raised by the decision in this case. Instead, they assign as reasons for granting the petition for a writ of certiorari that the issue is of tremendous importance both legally and economically; that the adverse effect of the lower court's decision is critical; and that the decision defeats the purpose of the Bankruptcy Act and the intention of Congress. An examination of these reasons will reveal that they are basically without merit, and that they do not afford any compelling reason why certiorari should be granted. The instant case has decided an issue of fact and law arising under the peculiar facts of this case, and the application of the Pennsylvania law with respect to the relative priority of liens between a landlord and a chattel mortgagee. Security transactions under the Uniform Commercial Code are not at all affected by the decision of the court of appeals. The chattel mortgages here in question arose before the adoption of the Uniform Commercial Code, and were given pursuant to the provisions of the Pennsylvania Chattel Mortgage Act, supra. Every lender who took a chattel mortgage under the Pennsylvania Chattel Mortgage Act knew that in order to have a lien on the

chattels which would be superior to a landlord's lien in the event of a distraint for rent, it must first obtain a landlord's waiver of the landlord's right to distrain on the mortgaged chattels. The Petitioners in this action failed to obtain such a waiver. It is inconceivable that they were unaware of this requirement of the Pennsylvania law. It is suggested that the real reason for not obtaining the landlord's waiver was the refusal of the landlord to execute such a waiver. The petitioners therefore assumed the risk of having their security impaired if the landlord distrained for rent.

The briefs filed in the court below by the amici curiae on behalf of certain banks, and the National Commercial Finance Conference, Inc. concerned themselves with the first opinion of the court of appeals, which held that in Pennsylvania a chattel mortgage was a "statutory lien" within the meaning of the Bankruptcy Act. This holding of the court of appeals has been cured by its action in withdrawing its first opinion, and writing a second opinion, which, although it reached the same conclusion as to priority of distribution of the funds, held,

> "It is not necessary to decide whether or not a Pennsylvania chattel mortgage is a 'statutory lien' within the meaning of Section 67, sub. c * * *. For the purposes of this opinion, however, we shall assume that it is not a 'statutory lien' within the purview of Section 67. * * *"

The amici curiae have thus accomplished their purpose. We are not here concerned with the law of other states, insofar as it relates to the priority of liens as between landlords and chattel mortgagees. In Pennsylvania, a chattel mortgagee can assure its superiority over the landlord, and thereby avoid the problem presented by the instant case by the simple expedient of being selective in its lending, and insisting upon obtaining a landlord's waiver of his right to distrain on mortgaged chattels.

The petitioners also argue that the holding of the court

below has already been extended in a Referee's unreported opinion in the matter of in *re George Townsend Co., Inc.* (reprinted in petitioners' appendix, p. 47). Petitioners admit that the facts in that case are substantially different from the facts in the case at bar. There, the landlord had *not* distrained and therefore had not perfected his lien on the goods pledged under the chattel mortgage and conditional sale. Petitioners state, "The Referee felt that the instant case compelled the result that under state law the landlord's claim, though not a lien, was entitled to priority over the security interests," and ordered distribution accordingly. It is obvious that if the landlord's claim was not, in effect, a lien superior to the lien of the security interests, then the decision in the case at bar does not apply. A reading of the referee's opinion discloses that he was inconsistent in his reasoning and decision. At page 48 of petitioners' appendix the referee says:

> "(2) Does the fact that the landlord did not distrain before bankruptcy in this case, change the order of distribution as promulgated in the Quaker City case, where there was such a distraint? I think it does. * * *"

The referee then proceeds to enter an order inconsistent with his own reasoning. If the Referee in the *Townsend* case was in error, the remedy lies in correcting that error and not in upsetting the clearly correct decision of the court of appeals in the instant case.

The petitioners' final argument for the granting of a writ of certiorari is that the decision in the instant case defeats the purpose of the Bankruptcy Act and the intention of Congress. Quite the contrary is true. The intention of Congress, as clearly expressed in the Bankruptcy Act, is to accord administration expenses and wage claimants a priority of payment over the landlord, whether the lien arising from the distraint for rent is statutory or not. The Congress, in its wisdom, has seen fit to grant priority to administration expenses and wage claimants over the landlord, in spite of

any state law to the contrary. The court of appeals in this case has given effect to the clear mandate of the Congress by holding that administration expenses and the wage claimants are to be paid before the landlord is paid. The petitioners' real position is that although they have failed to properly protect themselves in accordance with the established law of Pennsylvania, the state wherein their lien arises, by not obtaining a landlord's waiver of his right to distrain on the mortgaged chattels, this court, for extraneous reasons not connected with the issue herein presented, should issue a writ of certiorari, and thereby advance their interests. It is obvious that such a result is unwarranted.

VII. CONCLUSION.

The petitioners have conceded throughout this case, before the referee, before the district court, before the court of appeals, and even before this court, that under the law of Pennsylvania the landlord's lien is superior to their lien. On Page 13 of their petition, they state:

> "It is manifestly clear from a reading of the Bankruptcy Act that contractual or consensual liens *valid* under state law were to be so recognized and treated in the administration of a bankrupt's estate". (Emphasis supplied.)

This is the crux of the matter. What they have failed to say, however, is that the priority of the valid liens is established by the state law. Since they have conceded that under the state law their lien is subordinate to the landlord's lien, it becomes increasingly obvious that the decision of the court of appeals is correct. The Bankruptcy Act specifically postpones payment of the landlord's lien to payment of administration expenses and wage claims. The real position of the petitioners is that the mere act of bankruptcy has defeated the priority of liens established by the state law, even though the state law is the basis for their lien. The

court of appeals rightfully rejected this contention. The Congress did not intend, nor does the Bankruptcy Act provide that a petition in bankruptcy should create a superior lien where there was none under the state law before the petition was filed.

For the reasons herein set forth, the petition for a writ of certiorari should be denied.

Respectfully submitted,

DAVID GOLDBERG,
VERLIN & GOLDBERG,
Attorneys for Respondents,
1011 Finance Building,
Philadelphia 2, Penna.

VIII. APPENDIX.

Section 1. Act of Assembly (Pa.), June 12, 1878, (43 Purdon's Penna. Statutes 230).

It is the true intent and meaning of the provisions of the act of assembly, entitled "An act for the better protection of the wages of mechanics, miners, laborers and other," passed the ninth day of April, 1872, that the several classes of laborers in said act mentioned shall have a preference over landlords, in all claims for rent of any mines, manufactories or other real estate, held under lease, where the lessee or lessees are the parties employing the miners, mechanics, laborers or clerks: Provided, That any person or persons claiming a preference as above provided, shall give notice of the nature and amount of his claim to the landlord or his bailiff, before the actual sale of the property levied upon.

Title and Section 1 of the Pennsylvania Chattel Mortgage Act, (21 Purdon's Penna. Statutes 940.1 et seq.).

Relating to chattel mortgages on any chattel or chattels of any kind or description, including, but not limited to, livestock, poultry, farm machinery, farm equipment and crops, grown, growing or to be grown; designating the operation and effect of the lien of such mortgages; providing for the filing, indexing and docketing of such mortgages and related instruments in prothonotaries' offices; and prescribing prothonotaries' fees; providing for the filing in Pennsylvania of similar lien instruments originally filed or recorded in other states; regulating the assignment, release, satisfaction and extension of the lien of such mortgages; prescribing methods of foreclosure; defining defaults and violations; and fixing penalties.

Section 1. Any person, association, partnership or corporation *may* give as security for any funds borrowed or to be borrowed or any pre-existing indebtedenss, a bond or note, with or without a confession of judgment clause, secured by a chattel mortgage upon any chattel or chattels of any kind or description, including, but not limited to, livestock, poultry, farm machinery, farm equipment and crops, including annual or perennial crops, and other plant products, either grown or growing at the time of the execution of such chattel mortgage, or to be planted or grown within one year thereafter. For the purposes of this act all such chattels and crops shall be deemed to be personal property and mortgageable as such. The indebtedness secured by any such chattel mortgage shall not bear interest in excess of the rate which the creditor is permitted by law to charge at the time of the execution of such mortgage. (Emphasis supplied.) (Repealed by the Uniform Commercial Code—Secured Transactions, Act of Assembly (Pa.) of April 6, 1953, Public Law 3, 12A Purdon's Penna. Statutes, Section 10-102.)